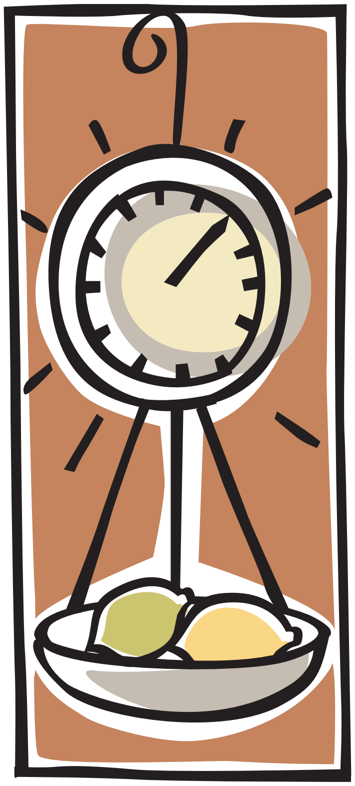

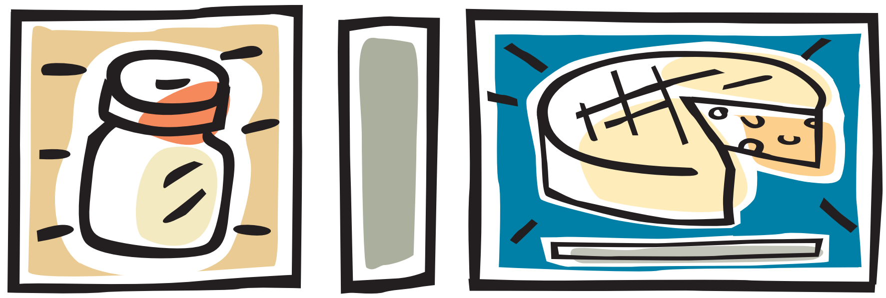

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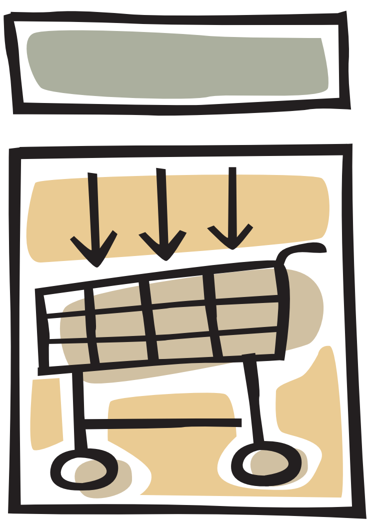

Food Co-op

by the Cooperative Grocers' Information Network

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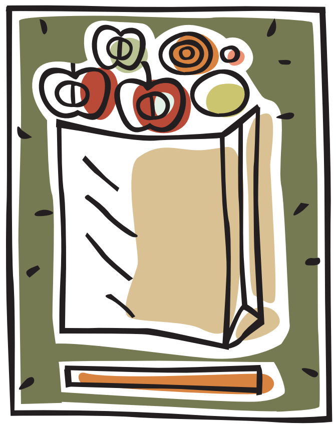
How to Start a



Food Co-op

A guide from the
Cooperative Grocers' Information Network

adapted from the original by
Patricia Cumbie and Margaret J. Goldstein
Cooperative Grocers' Information Network

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Introduction

Starting a food co-op takes a lot of work. But the rewards are many. This book provides an overview of the basic steps and procedures. The manual is not an exhaustive or comprehensive reference document. Groups interested in starting a new co-op are strongly encouraged to check additional references, including those listed throughout the manual.

Starting a co-op is a challenging and immensely rewarding activity. It will require research, careful planning, patience, and uncounted hours of time from you and your members. The co-op may not turn out exactly as it was originally conceptualized. It will inevitably take longer than you wish it would to get started. But when you invest the time and hard work to start a co-op, you will realize abundant benefits. You will learn about business and develop new skills. You will learn how to run productive meetings. Your co-op will provide jobs and meet daily needs in your community. Most rewarding of all, you will become a co-owner, with many others, of a dynamic and valuable business.

Good luck!

CHAPTER 1

Co-op Basics

Cooperation is a simple idea: two or more people join forces to accomplish something they probably couldn't do alone. People work together in thousands of ways each day. For example, parents take turns watching one another's children so they can do errands, work, or have time alone. Farmers traditionally helped one another with barn raisings and at harvest time. By combining their efforts, sharing responsibilities, and joining forces, people are able to accomplish many things.

A cooperative is a group of people who work together for economic benefit. Cooperatives bring the idea of cooperation—working together—to the business world. The cooperative idea has many applications. For instance, a group of parents might hire a teacher and rent a facility to create a preschool co-op. Individuals and families might pool their savings accounts to create a credit union. Whether cooperation happens through a cooperative or by individual action, the principle is the same. People working together can accomplish more than those working alone.

What Is a Co-op?

A cooperative is a business voluntarily owned and controlled by the people who use it—its members. It is operated primarily for the benefit of its members to meet their mutual needs. When many people have similar needs—such as the need for more affordable housing or for telecommunications services—cooperatives offer great potential to meet those needs.

At its core, a co-op is a business, and in most states co-ops can incorporate under cooperative statutes. Cooperatives have a different ownership and investment structure than publicly traded corporations, but cooperatives are not nonprofit businesses.

A cooperative has the same needs as any other business. Co-ops need sufficient financing, careful market analysis, strategic and comprehensive planning, and well-trained and competent personnel. Co-ops are not immune to the market and economic forces that cause small businesses to struggle and fail. But in several important ways, co-ops are different. Co-ops may resemble other businesses outwardly, but the fact that they are owned by members makes them unique.

Here is a simple definition of a co-op: "A co-op is a member-owned, member-controlled business that operates for the mutual benefit of all members and according to common principles established for cooperatives." More specifically:

- Co-ops are owned and controlled by those who use their services (the members).
- Co-ops are democratically governed.
- Co-ops are businesses, not clubs or associations.
- Co-ops adhere to internationally recognized principles.

There are three basic types of co-ops. *Producer co-ops* provide goods or services to members who make products, such as farmers or artists. *Worker co-ops* are owned and controlled on a democratic basis by their employees. *Consumer co-ops* provide goods or services used primarily by members for personal consumption. Food co-ops are typically organized as consumer co-ops. This handbook is written for those who want to start consumer-owned food co-ops.

FYI: Food Co-op Directories

Find a co-op in your area at: *http://www.cooperativegrocer.coop/coops* or contact Food Co-op Initiative to find a start-up in your area: *info@foodcoopinitiative.coop*

Philosophy and Principles

Co-ops worldwide share a common creed. They share a fundamental respect for all human beings and a belief in people's capacity to improve themselves economically and socially through mutual help. This basic philosophy has been developed into a list of seven principles that serve as guidelines for how cooperatives do business. Two of the seven principles describe who owns a co-op; two describe how decisions are made; and three list specific ways that co-ops put their beliefs into action.

The principles were originally developed in the mid-1800s by groups struggling to provide unadulterated, quality food at fair prices at a time when the market offered few options. As times have changed, the principles have been modified slightly, but the basic concepts have remained the same for more than 150 years.

In the 1990s, the International Co-operative Alliance (ICA) reviewed the cooperative principles and reformulated them. The modern co-op principles are:

1. **Open and voluntary membership (ownership)**
   Co-ops do not limit, for any social, political, or religious reason, who may join and become a co-owner of the co-op. Co-ops are open to all who can make use of their services and are willing to accept the responsibilities involved.

2. **Member economic participation (ownership)**
   This principle combines many concepts, all based on the basic idea that co-ops—and their money—are owned and controlled by their members. Members provide the basic capital (money) to start and operate the co-op. If co-ops pay dividends to their member-owners, the rate must be limited. Surplus, or profit, resulting from the operations of the co-op belongs to the members, and they control how it will be distributed. If a co-op's surplus is returned to members, it is distributed in proportion to the amount of business each member has conducted with the cooperative.

3. **Democratic member control (decision making)**
   All co-op members have equal voting and decision-making power in the governance of the business, on the basis of one vote per member.

4. **Autonomy and independence (decision making)**
   Cooperatives are independent, self-help organizations controlled by their members. They limit the influence of outside agencies or business partners to ensure their independence.

5. **Education, training, and information (special practices)**
   Co-ops have an obligation to educate members about cooperative business. This mandate also encompasses educating the general public, young people, and community leaders about the nature and benefits of cooperation.

6. **Cooperation among cooperatives (special practices)**
   To bring the theory of working together full circle, co-ops recognize the vital importance of working with other co-ops—locally, regionally, nationally, and internationally. Through these efforts, co-ops try to help each other—to strengthen their economic positions and to contribute to the co-op movement. This principle of "cooperation among co-ops" extends the idea of working together to the organizational level.

7. **Concern for community (special practices)**
   While member needs are their primary concern, cooperatives also work for the sustainable development of their communities.

In addition to reformulating the co-op principles, the ICA created the following "Statement on the Cooperative Identity." Approved by ICA members in September 1995, the statement defines the standards by which all co-ops should operate:

> Cooperatives are based on the values of self-help, self-responsibility, democracy, equality, equity, and solidarity. In the tradition of their founders, cooperative members believe in the ethical values of honesty, openness, social responsibility, and caring for others.

Co-op Governance

In the corporate world, the board of directors is responsible for a corporation's actions and for ensuring that the business is managed soundly. The co-op world is no different. The co-op board of directors is an elected body responsible for overseeing the affairs of the co-op on behalf of the owners (members). The board must act as whole; individual directors have no authority outside of board meetings, except as delegated by the board as a whole. Generally, only members in good standing may serve as directors of a cooperative.

State law defines the basic roles and responsibilities of a board of directors. Most commonly, state statutes say that a board member is required to act "in good faith, in a manner he (or she) reasonably believes to be in the best interests of the corporation, and with such care as an ordinarily prudent person in a like position would use under similar circumstances." All directors are required to meet this standard.

Directors have three primary responsibilities:

- To act as trustees on behalf of the members. Directors do this by carefully monitoring the co-op's financial status, hiring auditors to review financial records, reporting on the status of the co-op to members regularly, and making sure the co-op follows its bylaws, policies, and appropriate regulations.
- To ensure sound management of the co-op. Directors are responsible for hiring and supervising the co-op's management. Supervision includes reviewing management reports, monitoring key indicators (such as inventory turnover, sales trends, and other financial ratios), and evaluating management performance.
- To set long-range goals and plan for the co-op's future. Directors do this by holding strategic planning sessions, approving yearly and long-range plans, and setting performance goals.

The board is accountable to the members. It hires management, and management is accountable to the board. In some cases, directors may wish to contract with consultants or have volunteers to do some work on their behalf. Effective boards avoid micromanagement. They focus their discussions and decision making on two things:

- Clearly defining results to be achieved by management or others responsible for a project
- Setting limits needed to guide management's performance

Most boards meet monthly or at regular intervals. Boards elect officers—president, vice president, secretary, and treasurer—to organize and coordinate their work. Effective boards get regular training to make sure directors understand and can fulfill their responsibilities. Boards that stay focused on providing overall direction and monitoring the co-op's performance play a key role in the success of every co-op.

case study

Friendly City Food Co-op

Harrisonburg, Virginia
www.friendlycityfoodcoop.com

In the Shenandoah Valley, near Shenandoah National Park and the Blue Ridge Parkway, you'll find the "friendly city" of Harrisonburg, Virginia, a town with 40,000 residents about two hours away from Washington, D.C. It's a place where cultural food traditions run deep but also where mass food production has been long established. Harrisonburg is an agricultural town with a mix of family farms, feed mills, and big poultry processing plants. The town also has two colleges, a state university, and a Christian academy. It has several conventional chain grocery stores and two small independent health food stores focused on supplements. Residents wanting natural foods and high-quality dining have long been underserved.

In 2005 the Little Grill, a worker-owned restaurant, attempted to launch a natural foods store in Harrisonburg. When the store started to struggle, its owners sought help from a group that had expressed interest in starting a food co-op. That group realized that Little Grill's store was not a viable venture: it was too small and didn't offer what the community really needed. The store closed, but its closing jump-started the process of establishing a full-service food co-op in Harrisonburg.

In the fall of 2006, organizers hired a consultant, an expert in food co-op development and expansion. With his assistance, they began to understand what they needed to do to make the co-op a reality. The job was daunting. The group needed to raise more than $1 million from co-op members. In early 2007, organizers held their first fund-raising gala. The party's success went beyond their expectations. People came out in droves on a cold February night, enjoying good food and music. Almost 100 people joined the co-op that evening. People were excited about the possibility of having a food co-op in their community. The event gave the founding group resources and momentum to keep going.

That doesn't mean the organizers didn't hit snags. They eventually realized they'd fallen in love with a totally inappropriate site. A co-op site and location specialist encouraged them to abandon it in favor of something more visible and with adequate parking. The search for a good site dragged on. And because it had no new information to pass on, the founding group stopped communicating with the community. That was a big mistake, according to one founding member, because "people thought we were up to no good" or that the co-op was "dying." Consultants told the group to put more effort into communications, not less, even if it was to report nothing new, and to continue to ask people to be part of the co-op.

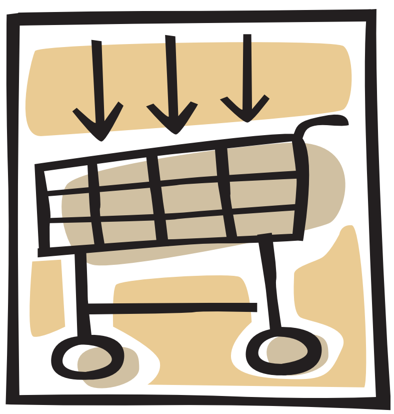
The founders launched a membership drive and ramped up their outreach. This activity brought fresh energy to the project and gave them the pool of members they needed to raise adequate member loan dollars. They hired someone to work 10 hours a week on administrative tasks and event coordination.

When they were finally able to secure a lease on a store, the organizers went into overdrive to raise member loans. They e-mailed, telephoned, and threw more parties to raise more money. By the fall of 2010, the group was on track to meet its goals for membership recruitment and member loans. It had hired an experienced food co-op general manager to establish operations.

Looking back, Friendly City Food Co-op organizers offer this advice for other start-up food co-ops: Things often take longer than you think; don't get ahead of yourself. Pay attention to planning and preparation. Speak to co-op professionals as soon as you can. You'll have to pay for advice, but professional services will save you time and money in the long run. Hire a staff person to get more work done and to create an environment of accountability and follow-through.

Friendly City Food Co-op at a Glance

Year incorporated:	2007
Projected opening:	2011
Number of projected members at opening:	1,200
Number of members in 2010:	1,035
Member equity investment:	$200
Cost of total project:	$1.8 million
Member loans:	$700,000 (goal of $950,000 by 2011)
Member equity:	$200,000 (goal of $240,000 by 2011)
Financing:	$500,000
Retail square feet:	4,200
Projected first-year sales:	$2.5 million



CHAPTER 2

What Is a Food Co-op?

In simplest terms, a food co-op is a business that buys food and household items for its members. The co-op helps members obtain high-quality products at the best possible price. Food co-ops offer consumers a retail environment free of coercive sales influences and with full disclosure of product quality and value.

Food co-ops typically operate retail stores. Many food co-ops offer a wide range of products and services aside from groceries. These might include cooking and nutrition classes, housewares, and catering.

Most food co-ops are open to anyone who wants to shop at the store, although stores may provide special services, prices, or benefits to members only. Any shopper can become a member by joining the co-op, which usually involves making a one-time equity investment.

Approximately 350 food co-ops operate in the United States. The majority of these stores primarily focus on natural foods. However, a number of food co-ops offer a full line of mainstream groceries in addition to natural foods.

FYI: Sources of Start-up Financing

- Co-op members (membership shares, donations, loans, equity shares)
- Fund-raising events
- Angel investors
- Self-directed IRAs
- Local economic development offices
- State minority and small business development offices
- Local chambers of commerce
- Small business development centers
- USDA rural development grants and loan guarantees
- USDA business and industry loan programs

Old and New Waves

Food co-ops in the United States formed in two distinctive waves. The Great Depression of the 1930s triggered the first wave. During this decade, families across the United States struggled to make ends meet. Many food co-ops launched in this period.

The story of the Hanover Co-op is typical. In the small town of Hanover, New Hampshire, families struggled to set aside just $8 or $9 per week for groceries. What fresh fruit and vegetables they could get were of poor quality and expensive. In 1935 17 local residents gathered in the town high school to discuss the idea of starting a consumer co-op. The co-op could help them reduce their grocery costs and buy products that were otherwise unavailable.

In January 1936, the group formally established the Hanover Consumers' Club. Negotiating for discounts with suppliers, the club began buying fresh citrus directly from Florida. Before long, the group was also buying bread, wine, canned vegetables, gasoline, and fuel oil. The club was successful and quickly outgrew its space in a basement garage. One year after it started, the co-op moved into a retail location. Its first-year sales were $11,400.

This story repeated itself in other U.S. towns, including Berkeley and Palo Alto, California; Eau Claire, Wisconsin; Hyde Park (a Chicago neighborhood); and Greenbelt, Maryland. Although most of the old wave stores have closed, the co-ops in Hanover and Eau Claire continue to operate to this day. You can visit their websites: *www.coopfoodstore.com* (Hanover) and *www.megafoods.com* (Eau Claire).

In the late 1960s and 1970s, the new wave of consumer co-ops began. Born out of the ideas and philosophies of the 1960s counterculture, these stores were opened by young and idealistic members. They set up co-ops to reflect their ideals about equality and justice and to provide unadulterated food. Most of the new co-ops sold only whole, unrefined, and bulk foods. Their operating practices were diverse and experimental. Some stores had limited hours; others were open seven days a week. Some were run by volunteers; others by fully paid staff. Some had various forms of worker self-management; others had more traditional management structures. Some paid year-end patronage refunds; others gave members discounts at the cash register.

These co-ops were pioneers in what came to be known as the natural foods industry. But not all were successful. Some failed because of their experimental structures and operating systems. Most were unable to escape the same problems that had troubled older, earlier co-ops—insufficient capital, inadequate membership support, an inability to improve operations as the grocery industry changed, a stronger commitment to idealism than to economic success, lack of adequate support from wholesalers, and resistance to consolidation. But the new wave co-ops that survived are strong and well established.

Interest in starting food co-ops has burgeoned in recent years. More and more people want the benefits that a food co-op can deliver. People want to contribute to a strong local economy and to local and organic agriculture. They want to patronize ethical businesses, build a more cohesive community, and obtain fairly priced, high-quality foods. Today, starting a food co-op is a much more involved endeavor than it was in the 1930s or the 1960s, since consumer expectations of food retailers are much higher now.

FYI: The Co-op Start-up Steering Committee

The steering committee is responsible for moving the co-op through its early stages, until more formal structures can be established. Depending on time and resources, the committee may do the following tasks itself or assign these tasks to outside professionals:

- Research and gather information
- Conduct a preliminary feasibility study
- Survey potential members
- Establish a membership structure
- Recruit members
- Explore options for financing
- Pursue initial inquiries with financing agencies
- Report on progress to members
- Hold membership meetings as needed
- Prepare a business plan
- Coordinate publicity and public relations concerning the co-op

Subcommittees might include:

- A planning committee to conduct a feasibility study; research locations and eventually handle real estate negotiations; research equipment sources, local regulations, and suppliers; and coordinate preparation of a business plan
- A finance committee to develop financial projections, research funding options, and coordinate a campaign for member loans
- A membership committee to research membership structures, prepare information about the co-op and the paperwork needed for membership administration, coordinate recruitment of new members, organize membership communications (newsletters, websites, letters) and meetings, survey members, and plan outreach to the community

Keep in mind that certain committee tasks require a level of confidentiality, responsibility, and follow-up. Depending on what you need people to do, be clear about roles and ensuring accountability.

Why Start a Food Co-op?

People start food co-ops for a wide variety of reasons. Some start food co-ops for access to unique or specialized product lines. Others open co-ops when privately owned or chain food stores close in their neighborhoods. People often realize that a locally owned store will better serve consumers' needs and will benefit the local economy and community more than a chain store.

Starting a co-op is just as complex and time-consuming as starting any business. To be done properly, it can't be rushed. Most experts estimate that starting a new co-op takes at minimum two years. As with starting any business, starting a co-op will involve thorough and careful business planning. Depending on circumstance, new co-ops will need to go through the following steps, although not necessary in the order listed:

- Gather background information
- Assess community interest
- Incorporate
- Organize within the community
- Recruit members
- Research feasibility
- Plan for financing
- Secure financing
- Select a site
- Prepare for opening
- Begin operations

Throughout the process of planning and start-up, keep several thoughts in mind. First of all, be patient. Allow plenty of time for people to meet and discuss ideas. Community building takes time, but it will create deeper and more widespread support for your co-op.

Look for resources specific to starting co-ops, including co-op development organizations, state and federal agencies, county extension offices, universities, and other local co-ops. Consultants familiar with the special laws and financial regulations applying to co-ops can provide invaluable experience and assistance. Be sure the lawyers, business planners, financial advisers, and development consultants you hire know what a co-op is and are familiar with the unique aspects of co-op operations. Also make sure to learn as much as you can about co-ops.

A new co-op has a better chance of succeeding and surviving if it begins by successfully operating only a store. Deli, bakery, and juice bar operations, while appealing, require additional and specialized expertise. Be careful about spreading your limited management talent too thin at first. Don't expand until you have experience and a successful track record to build on. Pay attention to business fundamentals. Studies have shown that the two main reasons for new co-op failure are insufficient capital and lack of business expertise.

case study

Dixon Cooperative Market

Dixon, New Mexico

www.dixonmarket.com

Dixon is a small, northern New Mexican village with a population of about 800. Located about halfway between the more sizable towns of Taos and Espanola, the village was established in the 1600s. It is primarily populated by Hispanic old-timers and Anglo newcomers.

Although it has a long and deep history in New Mexico, it has long been a rural and isolated community, with a population density of 22 people per square mile. For many years, Dixon lacked a grocery store. Residents had to drive either 20 minutes south to the supermarkets of Espanola or 20 minutes north to Taos, which has both supermarkets and a natural foods grocery.

The idea for a food co-op in Dixon came from one resident, who announced an open meeting for interested townspeople. From that meeting emerged a core organizing group of four people. Over three years, the organizers educated themselves, looked for a suitable retail space, and raised funds. They sold shares to members at the local farmer's market. They also received a $32,000 grant from the U.S. Department of Agriculture. The co-op incorporated in September 2003.

The organizers considered any and every open space in their small village to house the co-op. They eventually rented a portion of a vacant storefront next to the town library and across from the elementary school. The space was small—just 1,000 square feet—and required renovation work, which was supplied by community volunteers.

As the project proceeded, enthusiasm for the store grew. Organizers sought start-up advice from La Montanita Co-op, which operates stores in Santa Fe, Albuquerque, and Gallup, New Mexico, as well as from vendors and other small grocers. By 2005 the Dixon Cooperative Market was ready to open its doors.

The co-op now offers a full line of groceries, with an emphasis on locally produced foods, including fruit and vegetables, meat, spices, tortillas, and tamales. It is a hybrid store that offers natural foods as well as conventional groceries to meet community needs. Its small paid staff receives assistance from a team of dedicated member volunteers.

The co-op has evolved to become the center of Dixon's community life. On the veranda in front of the store, people hang out for hours, drinking coffee and meeting friends. Before the co-op opened, Dixon was a sleepy village, a mere blip on a map. Now it is a lively place with a farmer's market, music in the park, and a grocery store.

The small store is packed with products; the need for expansion is great. A potential space adjacent to the library would allow the co-op to double its size. The co-op has applied for a development grant to help finance the move.

The Dixon Cooperative Market's story is atypical of most start-ups; most need a greater base level of resources to be sustainable. But the people of Dixon have proven the cooperative idea can work for even the remotest of communities with few resources.

Dixon Cooperative Market at a Glance

Year incorporated:	2003
Year opened:	2005
Number of members at opening:	100
Number of members in 2010:	400
Member equity investment:	$200 or $25 per year
Cost of total project:	approximately $35,000
Member loans:	none
New member equity:	approximately $10,000
Financing:	$32,000 USDA grant
Number of staff at opening:	3
Number of staff in 2010:	5
Retail square feet:	1,000
First-year sales:	$126,000
2010 sales:	$500,000

CHAPTER 3

Member-Ownership and Equity

All businesses need capital (money), and a food co-op is no different. There are two basic sources of capital: equity (money provided by business owners) and debt (money provided by outside sources). In a food co-op, equity most typically comes from net operating surplus (profit) and from membership investments (member equity). Debt comes from loans, including capital leases, lines of credit, mortgages, and member loans. Each kind of capital offers advantages and disadvantages.

Member equity is money invested by members as owners of the co-op. Equity investments form the base capital of the co-op and may be refundable to members when they leave the co-op. When acquired properly, member equity is not a taxable source of funds for the co-op.

Food co-ops use member investments to purchase equipment, expand inventory, improve facilities, pay off debt, pay deposits with suppliers, and research new services and business opportunities. In today's economic environment, raising adequate member capital is critical to a successful start-up. Without sufficient member capital, a co-op may be unable to secure additional financing from outside sources, such as banks, suppliers, and other creditors.

Supplier credit is usually limited and can lead to higher prices. Bank financing is expensive and almost always comes with some restrictions. And bankers are often reluctant to lend money to co-ops that have inadequate member-owner financing or will lend them money only at high interest rates. When a co-op has an adequate capital base, bankers are more willing to make loans at reasonable cost and without imposing constraints on the co-op's operations or goals.

In a co-op, members provide capital by purchasing shares (just like purchasing stock in a publicly traded corporation). The share purchase is a requirement of membership. Typically, the board of directors sets the amount of shares that members must purchase. Making this investment gives each member the rights and responsibilities of co-op ownership.

Creating a Member Equity System

When putting together a member equity system, it is important to have a lawyer familiar with co-op securities law review all membership documents. Membership systems must comply with state laws governing cooperatives.

The co-op should set a reasonable investment requirement for all members. It should not require different levels of investment for individuals, households, seniors, low-income members, and so on. The co-op must also clearly define member shares as the *property* of members. If a co-op allows more than one individual on a single membership, the membership needs to be clearly defined as the joint (nondividable) property of those members. The co-op must avoid becoming an arbiter in property disputes. The co-op also needs to issue some sort of evidence of members' investment. Most co-ops use membership cards. Some states require membership certificates.

Member equity dollars are raised over time throughout the life of the organization. But planning for adequate equity from member-owners in the beginning phases of co-op development is critical. It's important not to limit your co-op's potential by setting member equity requirements too low. "Lifetime memberships" should also be avoided, since the co-op might need to change its investment requirements at some point. Co-ops should be realistic about future capital needs and set the share requirement to meet them.

Once you have set your member equity requirement, you can decide what type of payment plans to allow. This decision might come with much discussion and some anxiety. Payment options help make the co-op more accessible to potential members. However, co-ops should encourage full payment upon joining to save on administrative work and to maximize member equity. Suppose your co-op requires an initial share purchase of $200 with an option for $25 payments spread out over a long period. If most people choose the payment plan, you're not going to raise much money at the start. To encourage people to pay in full, consider charging an annual administrative fee ($3 to $5) for members making payments. Waive this fee for those who pay in full at the time of joining.

Member shares should be fully refundable upon termination of membership. But the co-op should make share repurchase contingent upon receiving replacement capital. Most co-ops total new share investments each month and pay repurchase requests up to that amount. This system helps co-ops avoid heavy seasonal outflows of capital. Most start-ups should not repurchase shares until at least two years after operations begin.

Keep your membership system simple, so members will be able to understand it and staff will be able to accurately explain it. Also keep administrative systems simple. New members should be eligible for all member benefits (including voting) as soon as their applications have been processed and approved.

For more information on setting member equity levels and creating a membership administration system, see the *Member Equity Toolbox: Structuring Capital to Meet Present and Future Needs* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox*. For information on signing up new members, see Chapter 5.

FYI: Sample Food Co-op Membership Structure

Member share requirement: $200. This share shall be a refundable investment by members. The required share investment will be the same for individuals and households. The $200 requirement will be made up of 10 $20 shares.

Joining: Upon joining, members must complete an application and pay for their shares. Members who make the full $200 investment at the time of joining will not pay a processing fee. Those who opt for the payment plan will pay a one-time $10 processing fee. Members will pay no additional fees to maintain active membership status.

Payment options:

1. Purchase the full share investment ($200) at the time of joining
2. Purchase 2.5 shares ($50) and pay the processing fee for a total of $60 at the time of joining. Pay the remaining $150 in three $50 payments.

Members may make investments ahead of schedule at any time with no penalty.

Eligibility: Individuals and organizations are both eligible to be co-op members.

Fees: Members will pay $5 for a replacement membership card, for reactivating a membership, or for repurchasing shares after termination of membership.

Repurchase: The co-op will repurchase members' shares at the board's discretion and only when it has received replacement capital. The co-op will total all repurchase requests at the end of each month and compare that total to the amount of equity invested that month by members. If new investment equals or exceeds the repurchase total, the co-op will send checks to terminating members. If not, the co-op will process repurchase requests in the order received, up to the total amount of equity received. The co-op will not repurchase shares until it has completed one full year of store operations.

Primary financial benefit: The board of directors may provide members with a patronage refund after completion of the fiscal year, depending on the capital needs of the cooperative.

Other member benefits:

- A vote in all co-op elections
- The ability to write checks for over the amount of purchase
- Member specials
- A monthly newsletter
- Reduced fees on co-op-sponsored classes and workshops
- Eligibility for membership at a local credit union

Member Loans

Member loans can provide the co-op with a good source of financing at reasonable interest rates. At the same time, they offer members a constructive way to financially support the co-op while also earning a decent interest rate.

Typically, a start-up will launch a member loan campaign after it has secured a site and recruited a substantial number of members. See “Financial Targets” in this chapter for more information about member share and equity benchmarks.

When setting up a member loan program, make it clear that only current members can make loans. Establish a minimum loan amount that is worth the paperwork and cost to the co-op. A suggested minimum is $1,000, with an average loan of $5,000. Establish interest rates that are workable for the co-op while also being attractive to members.

Consider interest rates that are equivalent to term CD or mutual fund rates. These rates will still be lower than what the co-op would pay for commercial loans. Give members the opportunity to loan money at various terms—with longer-term loans earning higher interest rates. Avoid member loans of less than five years unless the loans are just bridge financing until other financing can be arranged.

Interest payments on member loans can be handled in different ways. Initially, the co-op may wish to suspend interest payments (that is, have interest accrue only) until after one complete year of operation.

Do not pay back principal until the term of the loan has expired. Also stagger loans so they don’t all come due at the same time, which can cause serious cash-flow problems. When possible, set up a sinking fund for future repayment of loans.

Member loan materials should make it clear that member loans are unsecured. This means that no collateral (equipment, for example) secures the debt. Member loans are also subordinated debt. If the co-op has to repay loans, all creditors, bankers, and suppliers will get paid first, before the member lenders. Make sure an attorney familiar with co-op securities reviews all member loan materials, including brochures, offering memoranda, and promissory notes.

For more information on creating a member loan program, see Chapter 5. See also the *Member Loan Toolbox* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox*.

Financial Targets

Ensuring that your co-op has an adequate capital base to start with is key to its long-term survival. Two ratios can provide some guidelines for financial planning.

The *member-share ratio* is calculated by dividing total member investment by total assets. This ratio shows how much of a co-op's assets are financed by member investments. A benchmark for the member-share ratio is 20 to 30 percent.

The member-equity ratio is calculated by dividing total equity by total assets. This ratio shows how much of a co-op's assets are financed by equity (retained earnings and member investments). A benchmark for the member-equity ratio for an existing business is 40 to 60 percent. For start-ups, experts recommend that at least 70 percent of the asset base be provided by the co-op—either through equity or member loans or from donations, grants, or in-kind contributions.

The Patronage Refund

The cooperative idea is based on fairness. It is important to distribute member benefits equitably. In the past, some food co-ops offered member discounts at the register. Although popular, member discounts can cause serious drawbacks to a business. Essentially, co-ops that give discounts give away profits at the cash register before any expenses are accounted for. Overly generous discount programs have led to problems for food co-ops, including instability, loss of profit, minimal capital reserves, and business failure.

With a patronage refund system, a portion of the co-op's profits is returned to members based on their patronage, or purchases, with the co-op. The more a member spends at the co-op, the greater his or her rebate will be. At least 20 percent will be returned as cash. The remainder may be retained by the co-op as member equity to be used for improvements, future expansion, or overall financial stability. The patronage refund offers many advantages over the point-of-sale discount. Most importantly, it allows the co-op to know if it has made a profit before distributing a financial benefit to members.

It is the co-op's job to keep track of members' purchases to account for patronage refunds and retained equity. It is the board's job to refund profits, if there are any, and to decide whether they will be dispersed in cash or retained as equity. For more detailed information on patronage refunds, see the *Legal Primer on the Formation of Retail Consumer Food Co-op*s from the Food Co-op Initiative:
http://www.foodcoopinitiative.coop/resources/toolbox.

case study

River Valley Market

Northampton, Massachusetts

www.rivervalleymarket.coop

The journey to opening day at River Valley Market in Northampton, Massachusetts, highlights a community's tenacity and its earnest desire for a food co-op. One of the common challenges for start-ups is finding the perfect location. Either the real estate costs are prohibitive or there's nothing available. In a town where real estate prices are sky-high, River Valley Market experienced both problems.

The work began long before incorporation. In a strong, sophisticated, and competitive food market, organizers didn't want to rely on local volunteers to figure things out. They engaged the services of professionals to do feasibility and market studies. Research showed that the co-op idea was viable.

The co-op then set out to determine its member equity level. It surveyed other co-ops in the area about their equity requirements and kept accessibility in mind. It settled on a $150 share requirement. It decided that the person in a household who signed on to a share purchase would control it. That person would be the responsible party regarding benefits, voting, and informing the co-op of any changes to the household.

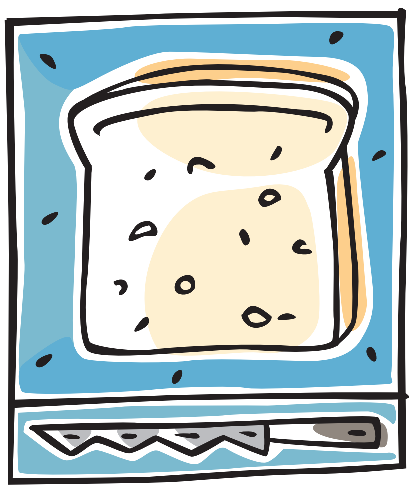
The co-op created a membership brochure, and a board member created a database to keep track of new members. But the sign-up system was cumbersome. New members had to fill out a paper application and mail it with a check to a post office box. For more efficiency, the co-op created an online application system. People could pay via credit cards with a PayPal account.

The co-op trained volunteers to sell memberships. It began a membership drive with a goal of getting 1,000 members. The co-op also created a member loan campaign with a goal of $1 million. Both the equity and loan goals were based on how much money the co-op needed to get financing for the project. The goals were reached, but not without their challenges. Because of the difficulty in securing a site, deals fell through one after another, and the group struggled with credibility in the community. Organizers needed to manage expectations and keep their messages about the co-op consistent.

Finally, after a number of feasibility and market studies, River Valley Market was able to lease an undeveloped property at a former rock quarry and build its store. The store opened in 2008 and is on track to meet sales projections. Not only that, leaders believe their co-op is well positioned to build community and participate in greater retail synergy in their area.

River Valley Market at a Glance

Year incorporated:	1999
Year opened:	2008
Number of members at opening:	2,000
Number of members in 2010:	4,000
Member equity investment:	$150 per household
Cost of total project:	$8.3 million
Member loans:	$1 million
Member equity:	$300,000
Financing:	$7 million
Number of staff at opening:	70
Number of staff in 2010:	75
Retail square feet:	17,000
First-year sales:	$8.1 million
2010 sales:	$10.5 million



CHAPTER 4
First Steps

Once you have the food co-op basics under your belt, you can take the first steps toward opening your community's own co-op. These steps including information gathering, community organizing, and research.

Step 1: Gather Information

Goal
To gather basic information about food co-ops and to assemble a leadership group to research feasibility and prepare the groundwork for starting a new co-op.

What to Do

- Gather basic information about cooperatives and how to organize a food co-op.
- Gather information about misconceptions about co-ops as well, so you can be prepared for some of the fallacies you may encounter in future steps.
- Discuss how a co-op could meet your needs with friends, neighbors, and others.
- Hold meetings to assess interest in the idea of a new food co-op and to inform potential members about how a co-op might work.
- Gather information about local and regional resources that may help your group, especially people who can serve as advisers, make presentations at meetings, and provide technical assistance.
- Collect basic information about operating a food co-op in your community, including the cost of retail space, health codes, and the market in your area.
- Contact food co-ops in your area or region. See what help they may be able to provide to your group.

Keep in Mind
This step will primarily involve a core group of individuals. The purpose of this step is to gather information and background that will be used in the next step, when you will publicize the co-op and try to gather and assess further interest within the community.

Key Decisions
Do we have sufficient information about how co-ops operate? Does the information we've collected justify further research? Does the co-op business structure fit our group's needs?

Step 2: Assess Community Interest

Goal: To assess whether there is enough interest in a co-op to justify further research and planning.

What to Do

- Hold an informational meeting of people who may be interested in a co-op. Publicize the time and purpose of the meeting as widely as possible—through your local paper, word of mouth, radio, websites, and so on. Make the meeting time, date, and location as convenient as possible.
- Plan a clear program for the meeting and select a meeting chair.
- Have someone explain the basic need for a co-op and discuss how a co-op might help meet that need. Give one or two simple handouts to all attendees. Handouts should summarize the basic idea and list names and phone numbers of core group members.
- Consider inviting guests who can provide public support or more detailed background information, such as directors or managers of other area co-ops, business leaders or educators familiar with co-ops, or elected officials.
- Allow plenty of discussion time, so people can ask questions and express their views. Be as clear and specific as possible but also be realistic about what the co-op can and can't do—especially in its early stages.
- Ask for participants to indicate their interest in the co-op by a show of hands.
- If there is interest, elect a steering committee to follow up.

Keep in Mind

Gauging interest and generating discussion about co-ops is important for knowing how much people understand about cooperation and whether or not they will support a store. This kind of outreach usually involves the efforts of numerous people. Coordinating communications will help your co-op conversation succeed. Conduct your outreach through:

- Community events and meetings
- Classes about cooperative ownership
- Direct mail
- Newsletters
- Social networking
- Websites
- Joining or partnering with organizations that share similar goals

Key Decisions

Is there sufficient interest in a co-op among potential shoppers and community members? Are people willing to work together to meet their common needs? Is there a clear need for a food co-op in your community?

FYI: Holding Successful Meetings

Before the Meeting

- Choose a convenient meeting time and location.
- Publicize the meeting using Internet communications, posters, displays at public events, and media announcements.
- Research the issues to be discussed.
- Clearly define the goals of the meeting.
- Arrange for a facilitator and note taker.
- Prepare a written agenda.
- Distribute the agenda ahead of time.
- Assign time limits for each agenda item.
- Limit the meeting to two hours.

At the Meeting

- Serve refreshments.
- Have someone greet people as they arrive and ask them to sign in. Collect contact information.
- Start the meeting on time.
- Have participants introduce themselves.
- Post the agenda or hand out copies.
- Review the purpose and goals of the meeting.
- Review the agenda and ask for any additions.
- End the meeting on time.

The Facilitator's Job

- Review the agenda and goals of the meeting. Get general agreement on the agenda.
- Set ground rules for appropriate behavior (no interruptions; make your comments concise; follow time limits).
- Keep discussions on topic.
- Encourage various points of view. Do not tolerate personal attacks.
- Ask people to speak for themselves. Discourage statements such as, "Some people think . . ." or "What she is trying to say is . . ."
- Cut off discussion if you don't have needed information. Appoint someone or a committee to bring more information to a future meeting.
- Make sure everyone has a chance to speak and that one or two people don't monopolize the discussion. Occasionally, check in with those who are quiet.
- If someone dominates the discussion, explain the importance of full group participation and call on others for comments.
- Take short breaks to relieve tension.
- Handle any voting needed. Before a vote is taken, clearly state the motion or proposal. Call for a show of hands. If the vote is close, have someone count hands or ballots.
- If the meeting is running overtime, have the group decide whether to extend the meeting or move some agenda items to the next meeting.
- Conclude the meeting on a note of achievement. Remind participants of actions taken and decisions made.
- Ask participants to evaluate the meeting and make suggestions for improvements.
- Remind the group of any follow-up needed for the next meeting.
- Remind participants of the next meeting time, date, and location.

Step 3: Formally Set Up the Co-op

Goals: To formally begin the co-op and accept the articles and bylaws (or basic rules).

What to Do

Prepare and Approve Articles of Incorporation and Bylaws

- Prepare basic rules that spell out who members will be, how much capital members must contribute, what the decision-making body will be and how it is to be selected, how decisions can be made, and how the basic rules can be changed. If the group has decided to incorporate, these rules will be spelled out in articles of incorporation and bylaws.
- Seek professional help, especially from those familiar with co-op laws, structure, and systems.
- Adopt and file articles of incorporation. Bylaws can be drafted and approved by a majority vote of the co-op's members later.
- File your articles and bylaws with the appropriate state agency.
- After approving the articles and bylaws, hold an election to choose the co-op's first board of directors.

Hold the First Board Meeting

- Elect officers: president, vice president, secretary, and treasurer
- Approve a membership application form
- Select a bank or financial institution
- Arrange for bookkeeping and handling of the co-op's finances
- Organize committees to pursue development of a business plan, financing and real estate negotiations, member recruitment, and preparation for operations.

Keep in Mind

At this stage, it is important to get expert legal assistance to review the articles and bylaws and to make sure that incorporation is compliant with federal and state laws.

The transition from the steering committee to governance by a board of directors can be rocky. Some start-ups create a founding team to take over for the steering committee after the first board election. While the new directors become familiar with governance and their legal responsibilities, the founding team can continue much of the hands-on work of preparing to open the store.

For information on incorporation, legal issues, and creating co-op articles and bylaws, see the *Legal Primer on the Formation of Retail Consumer Food Co-ops* available from the Food Co-op Initiative: *http://www.food coop initiative.coop/resources/toolbox*. For more information about the transition to governing, see the *Governance Toolbox,* available on Cooperative Grocers' Information Network (CGIN): *www.cgin.coop/toolbox*.

Key Decisions

Is the founding group ready to prepare organizing documents (such as articles of incorporation, bylaws, and membership agreements)? Do the articles and bylaws reflect the kind of business and the kind of cooperative members want to be a part of? Who will serve as the co-op's board of directors?

Step 4: Organize

Goal: To create basic organizational structures to move the co-op forward.

What to Do

- Establish a core leadership group to act as a steering committee.
- Choose a decision-making model for your organizing group, such as Robert's Rules of Order, super-majority, or formal consensus. The system will allow the group to move quickly through decisions and will provide a process for discussing disagreements.
- Establish committees. (Typical start-up committees include community outreach, finance, and membership committees.) Each committee should have a leader who sets meeting dates and reports to and communicates with the steering committee.
- Establish goals for committees. Review and revise them as necessary.
- Gather the names of people who may become members or co-op leaders.

Keep in Mind

This is a crucial and sensitive time for fledgling co-op groups. Deciding on and sticking to a decision-making model is absolutely vital for the success of start-up groups. It creates a foundation for communication and efficiency in later stages of co-op development.

For an overview of roles and tasks for steering committee members, see Chapter 2. For more detailed information, see the *Food Co-op Interest Survey Manual* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox*.

Key Decision

How will the steering committee and other committees make important decisions on behalf of the co-op organizing group?

Step 5: Research Feasibility

Goal: To assess whether the proposed co-op is likely to be successful and beneficial to its members.

What to Do

- Survey the community and prospective co-op members to identify common needs and the co-op's potential for generating sales. Conduct the survey by phone or face-to-face. Consider using professionals to assist with survey design and compilation.
- Collect and compile information. Learn about other co-ops in your area or region. Learn about similar businesses and how they operate. Identify possible sources of funding, including grants and loans. Get help from outside experts and consultants with experience in starting businesses and co-ops, including local university or business programs, co-op development organizations, chambers of commerce, and related groups.
- Conduct a feasibility study. The study should address the capacity of the market, the readiness of the group to carry out the project, basic financial needs and potential, and overall feasibility of the project. A professional market study is a key component of feasibility research.
- Prepare the feasibility report. Outside experts and consultants will be invaluable in preparing this information. Depending on the conclusions of your feasibility study, you may wish to hold another community meeting to report on the results and to make a decision about how to proceed.

Keep in Mind

While a food co-op may sound like a good idea, it is vital that you conduct a formal market study to make sure it's viable. A market study will help establish the general financial and operational parameters for your co-op, as well as the market capacity for your store. Don't base a feasibility study on overly optimistic assumptions.

To assess your plans, have an experienced businessperson review them and test your assumptions. If possible, compare your feasibility study or plans with those of a similar business. In the process, look for areas that you may have overlooked. Do your projections seem realistic? Do they prove the co-op's viability? Are potential sales assumptions tested and based on market data? Since a market study is a major expense, you may need financial support from potential members and other sources.

For more information, see "Key Elements of a Feasibility Study" in this chapter. See also the *Food Co-op Feasibility FAQ and Checklist* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox.*

Key Decisions

Is there enough interest in and sufficient market for a co-op? Is cooperation the best approach for this community? Does the feasibility study indicate that a co-op could succeed? Do the initial financial projections make sense and justify starting a new co-op? Do you have the skills and time needed to sustain a multiyear organizing effort? Can you raise the necessary capital to start the business?

Step 6: Review Findings

Goals: To present the findings of the steering committee, decide whether or not to proceed with starting a co-op, and gain the commitment of potential members.

What to Do

- Prepare a written agenda. Prepare copies of the steering committee's summary and recommendations to distribute to meeting participants.
- Send out notices to anyone who has indicated an interest in the co-op. Contact potential members by phone, listserves, and e-mail.
- Encourage interested members to bring other potential members.
- Make copies of a summary of the feasibility study plan and have them available for potential members to look over at the meeting.
- Present the steering committee's report.
- Allow members to discuss the report point by point. (It may be necessary to hold two meetings to cover the entire report.)
- Do further research or make changes to the steering committee report as necessary.
- After sufficient discussion, hold a vote of all potential members on whether to incorporate the co-op or abandon the effort. The resolution should designate the steering committee as responsible for preparing legal documents for the co-op.

Key Decisions

Are members ready to start a co-op? Are they willing to make a time or financial commitment to support the co-op?

FYI: Key Elements of a Feasibility Study

Common Needs

- What are the members' common needs?
- What products and services will the co-op provide?

Market Potential and Strategy

- What market capacity exists in the area?
- What kind of competition will the co-op face?
- How will the co-op distinguish itself in the market? How will it be different from competitor stores?
- Will the co-op benefit members financially? Are members more interested in other attributes of the co-op?

Operations

- How will the co-op be managed and staffed?
- What product lines and service departments are needed?
- Who are the primary suppliers for the co-op?
- What services will the co-op offer?

Financial Needs and Sources

- How much money is needed to get started?
- What will this money be used for?
- What are the approximate costs of operating the co-op?
- Will the co-op's operations justify and cover the costs, including debt service?
- How much money will come from members initially and how much from other sources?
- In the long term, how much will members have to contribute to the base capital of the co-op and how will it be collected?
- What are the options and costs for obtaining outside financing?

Start-up Needs

- How much time will it take to start the co-op?
- What management skills will be needed?
- What facilities will be needed? What will they cost and are they available?

For more detailed information, see the *Food Co-op Feasibility FAQ and Checklist* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox*.

case study

Eastside Food Co-op

Minneapolis, Minnesota

www.eastsidefood.coop

In the 1970s, a food co-op operated in the Northeast neighborhood of Minneapolis, a place characterized by new immigrants and long-established working-class families. The cooperative idea lingered in the neighborhood long after the store closed. In 1996 a group of Northeast residents got together to create a new co-op. That group signed up 135 members but eventually burned out when it couldn't find a workable location. Three years later, another group took up where the first one had left off. The first group turned over its equity to the second. The second organizing group worked on generating more community support. It knew it needed to be organized and systematic. It knew that predevelopment financing would be critical to its success.

After receiving a $20,000 grant from the neighborhood, the group commissioned a feasibility study. The study suggested that to be successful in the Twin Cities grocery market, the group had to open a full-service store—a project much larger in scope than organizers had originally anticipated.

The group hired a project manager to help find financing and a location. A co-op development consultant also began advising the group. It was difficult to find a site. In most places, parking was inadequate. The project manager was obsessively diligent, contacting every single landlord in the desired area.

Meanwhile, the group continued to connect with the community. It launched the Eastside Farmers' Market to help raise awareness of the co-op, build its network, and link residents to local fresh produce previously unavailable in the neighborhood.

In 2003 the co-op made an unsolicited offer on a building to a Boston-based owner. In March it made the purchase with loans from members and a neighborhood bank. The co-op opened later that year as a full-service grocery store, including a natural foods deli.

The first six months were tough. The co-op struggled and sales fell short of projections. But management held steady and worked hard to build sales. The challenge was to appeal to people unfamiliar with natural foods and co-ops while also welcoming those who did understand. Once the co-op became established, neighbors became more receptive. The board and management learned that word of mouth meant a lot. People began to talk up the store and encouraged others to come in.

In 2007 competition intensified when three chain grocery stores moved into the area. That year the co-op experienced only 2 percent growth. But the co-op has capitalized on its stature as the go-to place for community information, food education, and local foods. Sales have grown by 15 percent for each of the past two years.

Eastside Food Co-op at a Glance

Year incorporated:	1999 as a nonprofit; 2002 as a cooperative
Year opened:	2003
Number of members at opening:	800
Number of members in 2010:	3,085
Member equity investment:	$100 per two-person household
Cost of total project:	$2.1 million
Member loans:	$335,000
Member equity:	$80,000
Financing:	$1.1 million ($500,000 neighborhood, $80,000 other food co-ops, $7,500 co-op grant, $600,000 community bank)
Number of staff at opening:	28
Number of staff in 2010:	46
Retail square feet:	4,400
First-year sales:	$2 million
2010 sales:	$4.8 million

CHAPTER 5

Next Steps

Once the steps in Chapter 4 have been completed, the group will start to recruit members, create a business plan, secure financing, select a site, and prepare for opening.

Step 7: Recruit Members

Goal: To secure the written and financial commitments of members.

What to Do

- Research consumer co-op membership structures.
- Create a membership system. Be sure to address the member equity requirement, minimum payment required to join, payment options, additional fees, share repurchase (refund) options and limitations, and member benefits.
- Prepare a membership application and other materials needed for membership administration. Have an expert or attorney review these materials for proper representations and accurate, legal terminology.
- Establish goals for member recruitment and investment. Develop a method to track progress on those goals.
- Set up member record-keeping systems, including membership numbers.
- Prepare a simple, clear brochure explaining the membership system to potential members.
- Set up a website to accept membership payments and provide membership information.
- Develop a plan for member recruitment. Identify events and places at which to recruit members. Mail brochures and information to those who have indicated an interest in the co-op; use networks of existing co-op members and supporters. Publicize the co-op in the local newspaper, on the radio, and through other media outlets.

Keep in Mind

The membership structure is the foundation of your co-op. Carefully research membership systems and learn from the best practices and mistakes of other co-ops. Set up a system that will work for your co-op as a whole and for members individually. When creating membership materials, learn what words to use and what to avoid. For instance, members join by making an *investment* not paying a *fee*. Members may make payments to complete their share investments but are not *lifetime members*.

For more detailed information about building a strong co-op membership program, see the *Ownership Toolbox*, available on CGIN: *www.cgin.coop/toolbox*. For more information about how to set member equity levels and create a system for administering membership, see the *Member Equity Toolbox: Structuring Capital to Meet Present and Future Needs* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox*.

Key Decisions

Do we have sufficient membership commitment? Can we get sufficient financing from members to leverage further funding and keep debt costs within reason?

FYI: How to Conduct a Membership Drive

Raising equity for your co-op is serious business. Equity is the capital base from which your co-op derives its ability to grow. Your challenge is to educate yourself and potential members about this vital issue.

Involve others in the planning. Working as a group is crucial to success. People power, not the efforts of one person alone, will make it happen. Train a group in new member recruitment and make sure everyone gives a consistent message to prospective members. Communicate your plan enthusiastically through events and meetings, newsletters, handouts, and websites.

Set concrete goals and communicate them. Create a timeline, with goals for each development stage and an end goal in mind. Set goals that are high but reachable. Push for fully paid memberships to meet your goals.

Give free perks to new members upon joining. Offer a free shopping bag, a bouquet of flowers, or a coffee mug with your co-op's name on it.

Don't neglect support materials. Make sure you have adequate signage, banners, and brochures for your drive. These materials will convey your excitement to prospective members.

Make it easy to join. This is obvious but true. You'll lose potential members if joining is a hassle. If signing up takes longer than a few minutes, the process is too complicated. If necessary, create a script to help team members quickly explain co-op membership. Avoid too much paperwork and too many steps. Joining the co-op should be as easy as writing down your name and address.

Step 8: Create a Business Plan

Goal: To prepare a specific and detailed business plan for the co-op.

What to Do

Prepare a Business Plan

- Outline all aspects of the co-op's operations: who is involved, who the customers will be, what the co-op will sell, how it will operate, and how it will be capitalized.
- Determine the cost of operations.
- Conduct a professional market study.
- Hire consultants and experts with experience in business start-ups and preparing business plans and project work plans.
- Locate economic development programs and grants for start-up funding.

Report to the Members

- Prepare a report that summarizes the findings of business plan research.
- Present the summary at a membership meeting.
- Recommend whether or not to proceed with the co-op.

Keep in Mind

Deli, bakery, and juice bar operations are highly appealing and are generally viewed as desirable features of a new co-op. However, food production requires specialized equipment, facilities, and expertise. Consider leasing these facilities to other operators, at least initially.

For a list of key elements of a business plan, see "A Basic Business Plan" in this chapter.

Key Decisions

Does the co-op make sense from a business perspective? Do market studies and sales projections justify the co-op's plans? Does a business plan prove the co-op's viability?

FYI: A Basic Business Plan

A co-op business plan should include the following elements:

Introduction and Summary

- Name, address, and phone number of business
- Names and phone numbers of key personnel (management and board of directors or steering committee)
- Summary of feasibility research findings

Business Description

- Statement of purpose
- Summary of legal form
- Description of members
- Description of goods and services to be offered by the co-op
- Industry overview, including current status and prospects, new products and developments, and trends influencing the industry

Market Research and Plan

- Description of potential customers
- Description of market size and trends
- Analysis of the competition
- Estimated sales and projected market share
- Overall marketing strategy, including pricing, sales tactics, service policies, and advertising and promotion plans

Management and Development Plan

- Description of ownership structure, including required membership investment, member benefits, and projected membership size
- List of key personnel and organizational chart
- List of training, professional service, and staff needs and costs
- Development schedule, including projected costs, obstacles, and risks

Operating Plan

- Description of location and facilities
- Description of key suppliers and vendors
- Description of specific operational needs, including equipment
- Description of staffing system
- Analysis of critical risks

Financial Plan

- Five- to ten-year projections for profit and loss, cash flow, and balance sheet
- Break-even analysis
- Description of proposed sources of financing and cost of start-up (sources and uses budget)

Supporting Documents

- Resumes of those in the leadership group
- Letters of reference and support from key partners
- Membership applications and brochures
- Publicity generated by the co-op to that point

Step 9: Secure Financing

Goal: To obtain the funding necessary to finance the co-op's start-up and early stages.

What to Do

Secure Outside Financing

- Begin with capital from members for basic financing.
- Create a pro forma and a sources and uses development budget that includes key assumptions for the business.
- Research alternative financing, such as special start-up financing or economic development money for job creation or neighborhood revitalization.
- Contact local business or economic development agencies about their services for new businesses.
- Designate one or two people to negotiate with commercial lenders.
- Make sure potential lenders understand the cooperative ownership structure. With sufficient member financing and a clear explanation, individual guarantees should not be required.
- Contact potential suppliers about credit terms, opening orders, and technical assistance.

Create a Member Loan Program

- Research member loan programs from other co-ops and get sample materials from those co-ops.
- Determine how much the co-op will need in member loans. Based on that information, set limits on loan sizes and terms.
- Set interest rates for member loans.
- Put together member loan materials, including a brochure and a promissory note.
- Have an attorney knowledgeable in co-op and securities laws review your member loan program and materials. State laws differ, and you must make sure your program is legal.
- Publicize the member loan program among members.

Keep in Mind

For more detailed information about creating a member loan program, see the *Member Loan Campaign Toolbox* from the Food Co-op Initiative: *www.foodcoopinitiative.coop/resources/toolbox*. For more information about business planning and the role of lenders, see the *Expansions and Relocations Toolbox,* available on CGIN: *www.cgin.coop/toolbox.*

Key Decisions

Can the co-op raise the money needed to start up operations? Are the terms of loans and other credit acceptable to the co-op? Do projections show the co-op's ability to repay financing, even in less-than-ideal scenarios?

FYI: Potential Funders

Cooperative Fund of New England

http://www.cooperativefund.org

CFNE in Amherst, Massachusetts, makes loans to cooperatives, employee-owned businesses, and community-based nonprofits in New England and eastern New York.

Food Cooperative Initiative

http://www.foodcoopinitiative.coop

Food Co-op Initiative offers grants and loans to food co-op start-up organizations, as well as other resources, referrals and access to training materials.

National Cooperative Bank

http://www.ncb.coop

NCB has been providing loans to cooperative enterprises for years. It helps cooperative endeavors grow by crafting financial solutions and banking services tailored to each co-op's individual needs.

Northcountry Cooperative Development Fund

http://www.ncdf.coop

Located in Minneapolis, NCDF offers competitively priced loans to its members. NCDF has more than 170 member cooperatives and more than 200 individual members in 31 states. Any cooperative may join NCDF and apply for a loan.

U.S. Department of Agriculture

http://www.rurdev.usda/gov/rbs

The USDA funds development initiatives in rural and urban communities around the United States. Visit its website to learn about sustainability, food safety, specific grants, and funding.

Step 10: Site Selection

Goal: To find a location and site that will take advantage of retail synergy, attract a broad range of customers, and contribute to the co-op's long-term success.

What to Do

- Commission a professional location and site analyst with expertise in food co-op development to research the best place in your area for a retail co-op.
- Use the results of your feasibility and market study to learn about needs and shopping patterns of your prospective customers.
- Choose one or two people to handle site search and real estate negotiations.
- Explore options for leasing, owning, building new, or remodeling a site.
- Negotiate a lease or purchase agreement.
- Create an initial site plan and store design.
- Get preliminary approval from the city for the plans.
- Begin the bidding selection process for an architect and building contractors.
- Hire a project manager to oversee implementation after a site has been secured.

Keep in Mind

Location and *site* are not interchangeable terms. A location is the geographic place in your town that aligns your business with the right population and demographic profile. *Site* refers to the physical attributes of a specific place.

Understand that most real estate transactions require confidentiality. Without confidentiality, competitors could learn about or compete for the site. The deal might fall through. The involvement of too many people might affect the co-op's ability to negotiate effectively; conveying too much excitement might raise the price. Appropriate confidentiality will protect the co-op from potential liability.

Key Decisions

Have all the criteria for a good location and site been met? Have enough funds been raised to cover the cost of the project? Will the co-op sign a lease or a purchase agreement for the property?

FYI: Sample General Manager Job Description

Accountable to: The general manager is hired and supervised by the co-op's board of directors. The general manager serves at the board's discretion.

General Responsibility: To oversee the management of the co-op's affairs.

Specific Responsibilities:

Board and Member Relations

- Work with directors to prepare for and ensure productive, effective board meetings
- Present clear and timely reports and proposals to the board
- Follow up on board concerns and research issues in a timely and effective fashion
- Keep all directors informed about matters at and in between board meetings
- Establish systems and procedures that ensure that co-op members remain informed about the co-op's status, needs, and activities
- Monitor key indicators in the membership area and ensure new member recruitment

Financial

- Provide accurate financial statements
- Ensure that the co-op's assets are adequately safeguarded from loss
- Prepare all budgets and financial projections
- Perform in-depth financial analysis and promptly address financial problems
- Plan the co-op's financial future, including use of member equity, financing needs, and future profitability

Marketing

- Prepare comprehensive marketing plans, including regular analysis of the co-op's competition and market potential
- Ensure that the co-op is effectively presented to customers and its local market
- Use the marketing function to build long-term stability for the co-op
- Monitor and work to improve customer and member service levels

Operations

- Efficiently and effectively organize the co-op's operations to ensure profitability
- Identify and address operational problems in a timely fashion
- Plan for the co-op's ongoing operational needs, including technology, facilities, and equipment

Human Resources

- Establish personnel policies and procedures that support the co-op's values
- Ensure adequate training, evaluation, safety, and personnel systems
- Monitor personnel key indicators and plan for improvement as needed

Planning and Leadership

- Work with the board to ensure adequate planning for the co-op's future
- Provide leadership for the co-op through good communications, good business relationships, and good public relations

Step 11: Prepare for Opening

Goal: To prepare for the start-up of operations and to create the systems necessary for opening.

What to Do

Hire a General Manager

- Identify the skills you want in a manager.
- Write a job description for the general manager. Establish that the manager reports to the board, list the manager's first-year goals and priorities, describe how his or her performance will be measured and what compensation will be offered.
- Advertise the position as widely as possible. CGIN offers a Web page with job openings for co-ops: *http://www.cgin.coop/classifieds*. Advertise also in trade magazines, local papers, and employment offices. Also use economic development agencies, chambers of commerce, businesspeople, and other local co-ops to publicize the position. You may wish to consider hiring a search firm.
- Carefully screen all applicants. Check references and job experience in detail.
- Give preference to candidates with previous experience in retail operations or the grocery industry.
- Design an interview process that allows input from all interested parties but minimizes the number of interviews and interviewers that a candidate must face. Focus interview questions on the skills and experience a candidate has. Ask questions about how candidates have handled similar situations, not how they would theoretically handle a situation.

Transition the Board of Directors

- Train board members for hiring and managing the general manager.
- Clarify the responsibilities of the board, the general manager, volunteers, and hired staff.
- Develop a system for aligning expectations and planning for the future.

Keep in Mind

This stage can be tricky and somewhat traumatic. While the board and members have been heavily involved in operational decisions to this point, they will not be once a manager is hired. Allowing the board to remain involved in operational decisions will undermine the authority of the new manager. The board must craft and adjust to a new governance role.

For more detailed information about hiring a general manager, see *Hiring a General Manager: A Toolbox for Boards of Directors of Natural Foods Cooperatives,* available on CGIN: *www.cgin.coop/toolbox*. For more information about the transition from project to open store, see Chapter 6. For more information about the board's transition to governing and to managing the general manager, see A *Relationship of Respect: Evaluating Your General Manager* and the *Governance Toolbox,* available on CGIN: *www.cgin.coop/toolbox*.

Key Decisions

Is the co-op ready to begin operations? Does it have the expertise, experience, and resources needed for operations?

CHAPTER 6

Up and Running

Once management and facilities are in place, as well as a realistic budget and adequate capitalization (enough to cover operating losses for two to four years and negative cash flow for one to two years), the co-op is ready to begin operations. The board must transition to its new role. Management must set up staffing and other systems. Members must be ready to support the co-op with their patronage.

The Board Transition

Well before opening, the co-op needs to transition from the steering committee to the board of directors. Many co-ops facilitate this transition by creating a founding committee. It carries out certain tasks on behalf of the project while the board takes responsibility for managing the general manager and governing the co-op. Although some co-ops have crossover between the two groups, with some board members on the founding committee, the responsibilities of governance and managing project details must remain separate.

This separation is especially important when the board begins the process of hiring a general manager. In hiring the operational leader, the board introduces new roles and procedures into the organization. The board needs to learn how to effectively manage its one employee. It must understand that the general manager needs flexibility in creating an operating team and exercising authority as granted by the board. The board's relationship to the general manager has to be clear.

Many founding committee members and board members are accustomed to doing hands-on work on behalf of the co-op. The process of letting go and allowing others to develop co-op operations may unintentionally involve a struggle for control.

It is critical that boards get outside support and training for this process. Training will help everyone align expectations and plan for the future.

Managing the General Manager

The board must monitor the general manager's performance carefully in a start-up while at the same time extending trust during this period, a time when operations will create the foundation for the co-op's long-term success. The role of the board is to set a clear direction for the manager, determine management compensation, and monitor the general manager for outcomes. The board should expect the general manager to submit requested monitoring reports and to propose contingency plans regarding the co-op's operations and finances.

The general manager is the board's only employee, and it is important that the board and manager model the behavior and relationships they want to see manifested in the co-op. The board's role is to measure effectiveness, not general manager popularity—a point that's good to remember in a start-up, since the board will receive a lot of unsolicited feedback from the community and staff, especially in the early years. A strong understanding of the appropriate board-management relationship, and systems for feedback, will create an environment of fairness.

Monitoring Cash and Debt

As part of the oversight of member assets, directors need to evaluate the co-op's financial performance and make educated decisions based on solid information. This information is also an important tool for general manager accountability. Most financial information will come to the board as income statements and balance sheets. Comprehending this information will give you a much better understanding of the co-op's bottom line.

The first year in a start-up requires careful monitoring of cash position. Most co-op boards review financial statements on a quarterly basis, but in start-ups or co-ops experiencing cash flow problems or losses, the board might want to review monthly financial information. This information should include what was budgeted and year-to-date results.

In terms of cash flow and debt, the most common difficulty for start-ups is cash flow problems. The board and general manager should have a plan in place should the co-op not meet its projections. Worst-case scenario plans might include getting extensions on loans, negotiating terms with vendors, taking out a line of credit for inventory, or raising more member capital through member loans and membership drives.

From Project to Operations

Most people underestimate the amount of planning and work that goes into getting a grocery store operational. Even experienced grocers can be confounded by the process of starting everything from scratch. Every day untested systems need tweaking. Start-ups must be aware of the effort and commitment required to achieve smooth operational capacity. They must allow enough time for planning, implementing, and adjusting systems before opening their doors to customers.

Setting Up Operational Systems

The point-of-sale (POS) system, also known as the cash register system, is one of the most important operational systems in a food co-op, as are financial reporting and human resources systems. All these systems require technological sophistication and breathtaking attention to detail. Their setup and design is intricately linked to the long-term success of the co-op. Start-ups should hire a general manager at least six months before opening to get these systems in place.

Established food co-ops can offer a wealth of information on setting up operational systems. They can tell you what needs to be done and how to do it most efficiently.

Meeting Sales Projections and Managing Cash Flow

Concentrate operations on sales growth first, margin second, and labor third. Manage inventory carefully; for many departments, a monthly inventory will be necessary. Know what sells and what customers want. Adjust, monitor, and adjust some more. Get rid of inventory that does not sell and keep overall inventory as low as feasible while keeping the shelves looking good. Watch your cash, manage your cash flow, and plan for the day you run out. Be prepared to raise additional funds—via new members, member loans, lines of credit, and so on—if your pro forma budget was too optimistic. Be sure to set up systems for monthly financial statements.

Staff Training

An aggressive staff training program, before the store opens, will pay big dividends. The co-op will open with efficiency, with a head start in meeting customer expectations. Customers who have a positive experience on the first visit will likely return. Your training program will need to be multipronged, focusing on job performance, the co-op business model, and customer service.

Even though cash may be tight, your staff training program is an upfront investment in the co-op's success. After the doors are open, you will need to continue training and educating staff. It is likely that most people you hire will not have had much experience with cooperatives, or even grocery stores. So don't assume they've learned all they need after one training session. Do as much training as you can before the store opens and continue building staff knowledge and skills indefinitely. Monitor for burnout and provide an overabundance of praise and encouragement.

Make sure that staff members are prepared to promote co-op membership in addition to handling their store responsibilities. There is nothing like a successful and welcoming store to encourage new memberships, and investment from new members will be a welcome boost to the co-op's early cash flow.

FYI: Member Labor Programs—Evaluating Pros and Cons

As your work evolves from organizing the community to opening the doors of a retail store, you'll need to address the question of member labor programs, or volunteer labor. It is certain that a food co-op could not start up without legions of volunteers and supporters. Many co-ops want to maintain the enthusiasm and involvement of co-op members post-opening and may consider having their members volunteer in the store. This appears to be an attractive prospect: the co-op doesn't have to pay volunteers a salary for their work, an incentive during cash-strapped years.

However, many co-ops have learned that member labor programs are not necessarily a cost-savings boon. Someone has to coordinate and administer the program, and volunteers usually do not offer the same level of productivity and accountability as paid workers do. They cannot necessarily be relied upon to cover shifts, deliver good customer service, and follow food safety rules.

Some co-ops give volunteers a discount in exchange for their labor, but this practice raises red flags. First, giving discounts at the cash register before knowing whether the co-op is profitable can be financially harmful. Discounts tied to hours worked also risk being classified by the IRS as wages and subject to withholding taxes. Additionally, all grocery stores must comply with Department of Labor policies regarding workers' compensation, and most workers' comp doesn't cover volunteers.

Over the years, many food co-ops have modified working member programs. Some allow members to volunteer only at events separate from store operations and give them vouchers for hours worked. Other co-ops have discontinued working member programs altogether.

Despite the obstacles, some co-ops view member labor as a necessary part of their social mission and identity. Some stores have successfully managed to efficiently integrate volunteers into their operations. When evaluating whether a member labor program is feasible for your co-op, take into account liability, profitability, and operational efficiency to determine whether volunteers working in the store will be a good thing for the co-op.

Meeting Customer Expectations

Don't forget the crucial role of members in the success of every co-op. In the early months, keep in close communication with members—especially if it takes a while to get the store operating at full capacity. Let members know what is happening and when they can expect the kinks to be worked out. Make friendly service a top requirement.

Look at your retail operation from the perspective of your customers. Identify and promote goods and services that provide value to customers and prospective customers.

Cleanliness, convenience, product selection, and the way an organization conducts business all influence why consumers decide to patronize one store over another. Your challenge is to understand how important these features are to your customers and to deliver them to the marketplace.

Your customers are everywhere, inside and outside the business. Remember that a store might offer convenience, selection, and good prices yet fail to deliver through poor customer service. Research has shown that companies that emphasize service tend to be more profitable and have lower marketing costs, fewer customer complaints, and more repeat business.

Convenience

How easy is it to access and shop your store? Consider the store entrance, including the automatic doors and parcel pickup area. Look at the parking lot. Is it easy to enter and exit? Is the lot big enough to accommodate cars at peak shopping times? Does it have bike racks?

Are the checkout facilities efficient and accessible? Will the co-op bag and carry out groceries for customers? Are the aisle signs plentiful and readable? Is staff knowledgeable?

FYI: 'Tis Grand

Most stores have two grand openings. During the first, "soft" opening, you'll begin operations without much fanfare. Many of your first customers will be committed members. This low-key opening will allow you to test your systems and operations thoroughly. Your members will probably be a forgiving audience. Although the opening will be quiet, don't forget to celebrate your first sale. A few months later, you can throw a big, heavily publicized grand opening, complete with festivities and special events.

Products

Your product mix is a critical part of attracting customers to your food co-op. Customers will base their buying decisions on your product selection, price, and quality.

Evaluate your pricing on individual products, as well as department- and storewide pricing. Consider your price image. Are your prices perceived as high, low, or moderate?

Does your store offer variety? How complete is each department? Do you offer a mix of brands, package sizes, and bulk and prepackaged foods? Is packaging environmentally friendly? Is your repack area crisp and clean? Does the bulk area have bags and containers for self-packing?

Business Practices

Food co-ops often claim to be founded on ethical business practices, caring relationships, and ecological responsibility. How well are these traits communicated to customers and employees? Customer service and appropriate merchandising are your tools for conveying these messages to consumers. Customer service, following up on requests, and employee morale will show shoppers and the community at large the co-op difference. Store cleanliness counts, as does employee neatness. Pay attention to the store's interior decor.

Make sure the co-op operates ethically. What is your reputation in the community? What is the co-op's relationship to employees and the public? Does the co-op support charities and community events? Does the co-op actively educate consumers? Does it offer samples or cooking demos?

Promoting the Co-op

Promoting the co-op requires advanced planning that takes into consideration seasonality, products you want to promote, and your store's brand and price image. Promoting the co-op also requires good organization, accurate information, and good communication. Be aware of the impact promotional activities can have on many aspects of retailing. Promotions can help increase profitability, enhance departments, and build customer loyalty. As you plan ongoing promotions, keep these simple truths in mind:

- The natural foods industry is built on informed choice.
- An educated consumer can make informed choices.
- Customers are educated by information.
- If you inform people, they will develop loyalty to you.

As your operation grows, you'll probably need a team of people to launch product promotions. Your promotions may include active demos, advertising (in-store and through outside media), classes, direct mail, events, a newsletter, passive sampling, POS materials, public relations, raffles, sales flyers, social networking, staff education, and a website. Coordination and communication among staff are critical parts of successful product promotion

A Good Membership Base

Members are the foundation upon which a co-op is built, and it's important to continually and enthusiastically promote ownership in the co-op. Without a sufficient membership base, a co-op will flounder. Without a commitment by members to use the co-op, a co-op will be unable to survive. If members aren't willing to commit to the co-op, why should it exist? To assess your co-op's membership base, ask: What percentage of members' weekly food purchases are made at the co-op? What percentage of new shoppers join the co-op? What percentage of sales are made to members?

Looking Ahead

Six to nine months after your store opens, hold a planning retreat for management and the board to discuss how things are going and where to go next. Focus your planning discussions on the following year. Consider doing a member survey at this point—to make sure the co-op is meeting needs and to gauge members' satisfaction with the new store.

Be prepared for the rough road that many new stores face in their first year or so of operations. Opening a new store requires keeping many balls up in the air at one time. No matter how well you plan and train, some balls will inevitably come down faster or slower than you predicted. Don't allow yourself to be caught off guard when you encounter initial stumbling blocks. Be prepared to adapt and overcome them as they appear.

Eventually, after the first few years of operations, extend the co-op's planning horizon to three or five years. Remember that your co-op's ongoing success depends on constant attention to business basics and member communications.

case study

Just Food Co-op

Northfield, Minnesota
www.justfood.coop

The Just Food Co-op in Northfield, Minnesota, has celebrated its fifth anniversary, and what a milestone it has been for the community of 17,000. Northfield is a small college town about 40 miles south of Minneapolis-St. Paul. The population includes about 3,000 students from Carleton and St. Olaf colleges, two highly respected liberal arts institutions.

The co-op has become a focal point for people in the community. But this level of synergy and success did not always exist. Twice before, the Northfield community opened a food co-op only to see it struggle and close. But apparently the third time's the charm. Just Food Co-op will probably be celebrating many anniversaries to come. Now that it's passed five years, it's hard to imagine what things were like before Just Food opened. The co-op has become indispensible to the community.

The story of Just Food's development is a case study of what can go right when all the elements are in place: solid community commitment to the co-op, strong board leadership, and an excellent staff and general manager.

The community organized and opened a co-op in just two years. A critical point in the organizing process was signing up 330 members. Then, concurrent with its member loan campaign, the co-op set a goal of signing up 700 more members by opening. At that juncture, the Just Food founding group hired a professional to train them. With this assistance, the group was able to raise one-third of the needed financing through member loans and reach its membership recruitment goals. The founders poured themselves into organizing, attending countless community meetings and events to build awareness.

The co-op hired a human resources/front-end manager with a lot of experience in food co-ops. Prior to working at Just Food, she had been the human resources manager for a large co-op in Minneapolis. She later became Just Food's general manager. She figured that applying her skills to the start-up operation would be easy.

Not so easy, she soon realized. She had to hire nearly the entire staff at opening. She had to create all the systems and procedures needed to run a grocery store. The process was long and difficult. She was suddenly aware of a million details. "To come from a large co-op with these things already in place, it was a huge eye-opener," she says.

The manager trained all the cashiers (most of whom were inexperienced and unfamiliar with cooperatives), set up the POS system, created systems for cash handling and other front-end procedures, and created payroll, evaluation, and compliance-monitoring systems for the human resources department. If existing co-ops hadn't shared their systems and helped with advice, the task would have been nearly impossible.

The store hit cash flow problems in year two. It had to raise funds through C shares and aggressively encourage members to shop more. But perseverance paid off. In 2009 Just Food Co-op posted its first profitable year—a huge milestone for the co-op. Despite a tough economy, membership and sales continue to grow. Just Food is starting to talk about the future—possibly even an expansion.

Just Food Co-op at a Glance

Year incorporated:	2002
Year opened:	2004
Number of members at opening:	900
Number of members in 2010:	2,000
Member equity investment:	$125 per household
Cost of total project:	$1 million
Member loans:	$372,000
New member equity:	$112,500
Financing:	$390,000
Number of staff at opening:	28
Number of staff in 2010:	47
Retail square feet:	4,200
First-year sales:	$2.8 million
2010 sales:	$4.1 million

CHAPTER 7

Keys to Success

As with any new business, a number of factors enhance a co-op's chance to succeed. Paying careful attention to these items will help your co-op survive the tough first years. Review this chapter as a reminder and a recap guide to the information presented throughout this manual.

Do It Right

Communicate

Communication is critical when forming and operating a co-op. Good communication keeps members, lenders, outside advisers, directors, management, staff, competitors, and the community informed about the co-op's goals and accomplishments. Managers and directors must be good leaders. They must be well qualified and should pursue ongoing training.

To assess the quality of your co-op's communications, review information provided to members. Make sure it communicates how the co-op is doing as well as describing products and operations. Listen to members and shoppers at every opportunity. What items do they want to buy at the co-op? What do they like about shopping at the co-op? What would they like to see changed? It's certain that you won't be able to make all the suggested changes, but the two-way communication will be invaluable to your co-op. At the same time, be wary of a vocal minority that might want to dictate policy or restrict the co-op's operations. Remember that most co-op members "vote with their dollars" every day in the store.

Determine the Need for Capital

It can be easy to underestimate the costs of a start-up. Do your homework on how much it will cost to start the business and effectively pay off debt once it is open. You will need to develop a business plan (necessary to secure a loan) and get sound financial advice. Your financial needs will depend on up-front costs for purchasing a site, construction, remodeling, or leasehold improvements. Additionally, you will need capital for overhead, equipment, and inventory.

Food co-op start-ups typically raise at least half of their necessary capital from members. The rest comes from lenders and other sources.

You'll need enough working capital to keep the business afloat for the first 12 months, as well as a contingency fund and plans in case the business needs more capital. Experienced business managers know that being busy doesn't necessarily translate into a positive cash flow, especially in the first year, when the business has to make major purchases to get started.

Get Expert Assistance

Each co-op is unique, but a co-op can avoid making mistakes by learning from other groups' mistakes. Keep in touch with other co-ops; learn from their errors and accomplishments. Join the CGIN listserve to connect with other food co-ops. Join CGIN to access materials available only to members, such as sample job descriptions, newsletter articles, membership materials, and business plans. Read *Cooperative Grocer* magazine and other industry publications. Join other regional co-op or industry associations. Attend the annual Consumer Cooperative Management Association conference. Invite other co-op managers to your store for a simple store audit or to advise you or your department managers.

Also bring in outside expertise: business planners, co-op development specialists, consultants, operational experts, and attorneys. Advisers can help with legal and financial matters, industry and strategic planning concerns, and leadership training.

Plan for the Future

Your food co-op will need to undertake formal planning to realize long-term success. At the start-up stage, your plans should be based on realistic and valid assumptions. Since it is easy to become emotionally involved in co-op decision making, founding committees and boards should work hard to retain their objectivity during planning stages. Important planning activities include:

- A feasibility study. This study will give you an overview of start-up issues and help you decide whether a co-op might be successful in your marketplace.
- A business plan. If the feasibility study shows that the idea is solid, create a business plan for further analysis. The plan will help you secure a business loan and other investments.
- A market study. The market study will give you information about your target market, sales potential, and competition. It will also provide an analysis of a location and site.

Choose the Right Location and Site

Finding the best location and site for your co-op will take time and research. Remember that the "perfect" site doesn't exist. There are always tradeoffs, including cost, availability, and visibility. Choosing a site is one of the biggest decisions a start-up co-op will make. The decision will affect the co-op's ability to reach its sales goals. It is critically important to get professional assistance and conduct solid research before making a commitment to any location or site.

Hire Good Project and Store Management

Hiring a project manager during the planning stage and a store manager for the implementation stage will make the transition to operations smooth and efficient. Look for managers who are experienced in retail projects and grocery store management. Give your project and store managers plenty of time to plan and get systems up and running. Hiring these folks will pay for itself in efficiency and profitability.

Start-up Pitfalls

Every start-up project comes with unique challenges, but certain pitfalls are widespread. Review these common pitfalls so that your co-op can benefit from valuable past experiences, giving the start-up project an even greater chance for long-term sustainability and success.

Failure to Create a Culture of Respect and Accountability

Creating a strong organizational structure involves putting forth clear expectations for decision making, accountability for carrying out decisions, and strategies for communicating with stakeholders and the community. Co-ops without a well-structured board or organizing committee often waste a lot of time and sometimes send out mixed messages to the community, hindering their ability to gain widespread support. Groups sometimes must deal with dissenting opinions or inflexible personalities. Such issues can cause co-ops to get stuck or melt down.

Avoiding such pitfalls requires a high level of organizational leadership on the part of the co-op's founding group. How the founding group works together is indicative of everything else the co-op will do, and it can make the difference between taking only two or three years to open versus five or ten years. Professional advice, reference materials, and help with group process and facilitation will give you the tools you need to create a culture of respect and to build synergy and momentum.

Poor Member and Stakeholder Communication

Sometimes founding groups fail to report on their activities to the community of stakeholders. This oversight can result in too few people supporting the project, which can lead to failure. It's important to set up a means and a process for communicating widely and regularly. Vehicles can include community meetings, forums, outreach to other groups, websites, social networking, e-mails, and a newsletter.

Communication is critical in case of a setback, such as when a desired site falls through. People naturally put up barriers to communicating about a stalled project, fearful that others will lose faith in it. Certainly, some activities must be kept confidential, especially those regarding real estate and human resources. However, the last thing any group wants is a rumor mill disseminating inaccurate information about a project. Be transparent about your activities. Employ strategic and proper communication channels to help build trust with the community at large.

Jumping the Gun on Location

A start-up co-op might learn about a potential site or location and make it the impetus for an organizing process. This tendency is understandable, because it's a lot easier to organize a vision around something tangible than something intangible. However, groups should not get too far ahead of themselves regarding location.

In the beginning stages, the founding group should put its energy into planning, organizing in the community, and finding financing. It may be hard to put the idea of the perfect location on hold for awhile, but it is critical that groups do due diligence before getting involved in any kind of real estate transaction. Making any contractual commitments to real estate without having the money for it up front can put groups under tremendous pressure. Not only that, after some research or a market study, that "perfect" location may not seem so great after all.

Not Creating a Meaningful Work Plan or Reporting Structure

All groups need benchmarks and accountability. They provide concrete ways to monitor progress and allow activities to be carried out more efficiently. A work plan allows a group to achieve essential benchmarks in appropriate steps. Without a work plan, timeline, and reporting structure, a group might either take too long or rush into making decisions. Obtaining professional assistance with a work plan will make it easier for the co-op to systematically achieve its goals.

Not Involving the Community

Sometimes a core group feels passionate about starting a food co-op, confident of its success, but has not done enough research or outreach to know whether the community will use or support the co-op. It's critical for founding groups to keep an open mind about what the food co-op may mean to others. It's important to get adequate information, input, and support from a wide range of people and organizations.

This point cannot be overstated. While pockets of people in an area might desperately want a food co-op, it may be a tough sell in the greater community. Food co-ops that open without engaging the community often open with low visibility. They suffer from low customer counts and small average sales and are hard-pressed to survive.

Not Obtaining a Professional Market Study

Getting a professional market study is imperative to understanding a project's potential, but groups sometimes balk at doing it because it is expensive. A market study can cost upward of $10,000. In the organizing stage, it can be challenging to raise that money. Resist the urge to commission someone without expertise in the food co-op sector. Retail food co-ops are unlike any other businesses in terms of their approach to community ownership and business practices; working with someone who understands food co-ops can save a start-up group time and money and can mitigate the disappointment or disaster that can result from inaccurate information.

Boards have a fiduciary responsibility to their owners, and investors require reliable market study information. If you are working with erroneous information, your group may face the unpleasant task of altering your plan or paying for another study. You want a market study that a lender can accept with confidence.

Depending Too Much on the Founding Group

Because financial projections and market studies can be expensive, founders often look inward or cut corners to mitigate costs. Some groups skip the market study. Others hire professionals who don't have the right expertise.

Generally, start-up groups should get assistance from food co-op professionals for the following: financial projections, market studies, capital campaigns, board training, creating work plans, store layout and equipment planning, and operational preparedness. You will get the job done better and cheaper in the long run if you hire someone with experience in the food co-op sector.

Assuming It's Better to Start Small

The idea that it is better to start small is rooted in a historical perspective about food co-ops. After all, many of today's established co-ops started in churches, basements, or tiny storefronts. When these new wave food co-ops started forty years ago, there was no competition for natural foods. Health department and other regulations were not as comprehensive. It wasn't that difficult to meet the needs of a small customer base.

Today's grocery shopper demands a much more professional approach to food handling and merchandising, and most customers prefer one-stop shopping. It is hard for a grocery store to survive if customers cannot use it as a primary store.

Of course, it can be intimidating for a start-up to look at a budget for a multimillion dollar project, and groups might be tempted to scale back. However, if your area demonstrates market demand, starting larger may be the better option in the long run.

The risk of starting too small is that sales might not cover overhead (especially staffing), meet the needs of a variety of shoppers, or generate a big enough customer base. Especially where people have other grocery options—even limited options—small co-ops often struggle. In addition, a small co-op could run the risk of outgrowing its location too soon, necessitating relocation or remodeling and putting an added burden on finance and operations.

Not Heeding Advice on Best Practices

Nearly every group thinks its situation is different, and for this reason many are tempted to ignore best practices. Certainly, every group has its unique set of challenges, but it is likely that other co-ops have experienced something similar. For example, despite advice from experts, one group set its sights on a building with no parking, low visibility, and limited access. Organizers believed that shoppers would overlook those barriers because they wanted a co-op so much. The founders ignored professional advice because they thought their situation was different. Now the co-op is struggling to meet sales projections.

There are usually good reasons why certain things are deemed best practices. It's wise for groups to avoid decision making based on emotions and gut feelings and instead to focus on practices with a proven track record.

Opening with Inadequate Capitalization

A co-op needs enough working capital to get through the first year. The reasons are pretty obvious: you need to pay staff, buy inventory, and support the physical plant. Most new businesses have negative cash flow for a year or more and may not show a profit for several years. You can survive this rocky period with adequate working capital reserves. Opening without adequate capitalization with the expectation that you'll raise it as you go along is a big risk.

In a tough economy, demonstrating that a co-op has enough working capital to get financing is also challenging. The best strategy is to get advice on financial projections from someone with expertise in the food co-op sector and to have enough working capital before opening the store.

Settling for a Deficient Site

Some groups get frustrated and impatient with the site search when they can't find anything good in their price range. Some overlook site deficiencies (such as too little parking or low visibility) because a property can be had for a low price.

If you compromise on site, your co-op will pay the price with inadequate sales. Visibility and accessibility are shoppers' main reasons for picking a grocery store. Thinking a site will be "good enough" is actually an emotional decision, not one based on facts and consumer research. You will ensure your co-op's longevity by finding the best site for your needs, even if it takes a long time to find it.

Not Hiring Soon Enough

Your project will move forward faster, and with more professionalism, if you hire a project manager. Hiring this manager once you are past the initial feasibility stage is ideal. Even the most committed group of volunteers will not operate with the same level of decision making and accountability as a paid professional. Having a project manager signals to financial institutions and other stakeholders the seriousness of the founding group's intentions. A project manager will save you time during the implementation phase. His or her work can cross over with that of the general manager during the transition to store operations.

Some groups are lucky enough to find someone who is qualified as a project manager *and* a general manager, but this is rare. Both jobs require different areas of expertise. In addition, combining the jobs might cause inefficiencies in procedures, policies, hiring, and relationships with the board. It is best to open your food co-op with an effective team. It costs more up front but pays for itself in the long term.

case study

Boulder Cooperative Market

Boulder, Colorado

In Boulder, Colorado, a natural foods store called the Crystal Market closed in 1999. This left the community without a locally owned source for natural foods. Concerned patrons decided to form a co-op, the Boulder Cooperative Market, to take over operations in the same location. Organizers had only one month in which to act. That wasn't enough time to recruit members, raise money, obtain financing, and get ready to take over the facility. Organizers lost the chance to take over the store. But they were successful in collecting names of about 1,000 people interested in forming a co-op. A core group decided to pursue the idea.

In the next two years, the steering committee developed a feasibility study, built membership, wrote a business plan, found a location, and raised money. After making offers on three locations of 5,000 square feet or less, they found a 12,000-square-foot site with low rent. While the site needed lots of work, the group had many enthusiastic volunteers ready to pitch in.

The initial organizing group included about 40 people. Organizers borrowed office space and set up a campaign to recruit members by telephone. They called residents who had indicated support for the co-op at various community events, and they purchased the local Green Party's list of registered voters. In total they contacted around 3,000 people. More than 400 became members. Organizers followed up with newspaper and radio publicity and a website. Two local papers each donated $10,000 in advertising space. Other natural foods stores put up the group's posters. Over the next eight months, the co-op's membership increased to 800.

A market analysis concluded that the co-op needed at least 1,000 members who spent approximately $100 per month at the store, with about 30 percent of sales coming from nonmembers. The study projected that the co-op could break even at sales of $200 per square foot and that the location had the potential to achieve sales of closer to $400.

Communication was an important part of the organizing process. Organizers created a website and sent out a quarterly newsletter to update members on the co-op's progress. Funding came from member investments and loans, donations, a city grant, and lenders. A number of food manufacturers contributed product.

After opening its doors in October 2002, the co-op prospered for several years. By 2003 membership stood at 2,400. The co-op opened an adjoining restaurant, Café Prasad, and offered yoga and cooking classes.

But the co-op also encountered many obstacles that might have been overcome with better implementation and planning. Even before the store opened, the co-op spent a lot of money on building renovations. It created a debt load that it struggled to pay back, especially when sales dropped off.

The co-op was situated on a well-traveled road, but a dry cleaner and community bulletin boards fronted the business, limiting its visibility to passersby. The co-op had a lot of members, but over time it struggled to engage them. People quit shopping because service was disappointing. The co-op gained a reputation as insular and unfriendly.

It competed in Boulder with a Whole Foods Market, three Wild Oats Markets, and a Vitamin Cottage, as well as two Safeway supermarkets that offered some natural and organic products. The co-op was not well merchandized in comparison. Additionally, the co-op unwittingly focused on vegetarianism as its market niche. It sold no meat—a deterrent to customers seeking one-stop shopping, especially in a marketplace with many excellent choices. The co-op's strength as a local community-owned business went unrealized.

The co-op struggled with the reality of running a business and paying attention to the bottom line. Both board and management lacked necessary business skills. Budgeting was rocky, and cash flow analysis nearly nil. Sales declined and debt piled up. By the time people realized they needed to fix these problems, it was too late.

By the summer of 2007 the co-op was $1.5 million in debt. It couldn't pay vendors or stock shelves. In July 2007 the board of directors voted to shut the co-op.

Insiders say that proactive attention to issues typically facing a start-up might have helped the co-op stay afloat. Ultimately, lack of planning, undercapitalization, debt, poor management, and fierce competition spelled doom for the start-up co-op.

case study

Midtown Food Co-op

Memphis, Tennessee

In mid-April 2001, a national chain bought out Memphis's only natural foods store, as well as another natural foods store in the region. One of the stores was closed, leaving a number of area farmers without a market for their produce and leaving neighborhood residents with a long drive to a store that offered natural foods.

A group decided to open a neighborhood co-op to sell natural foods, bulk items, and locally grown produce. Once local interest was established, a core group held potluck dinners each week for six weeks. Members researched and discussed bylaws, possible sites, incorporation, potential vendors and distributors, and the role of the board of directors. By mid-June 2001, they had located a space for the co-op and signed a lease.

In June and July, the group prepared the store for opening. By that point, the core group had grown to more than 30 people. For the next two months, members gathered in work parties to tackle site preparation. Community members donated plumbing, construction, and electrical work. The group purchased $10,000 worth of bulk bins and kitchen equipment from another food co-op at a low price. The co-op wholesaler that serviced the area provided free shipping for the used equipment and assistance with planning and stocking.

Even in this short timeline, the co-op's organizers developed a business plan. They determined that with 1,000 square feet of selling space, the co-op would need to sell $25 per square foot per month, or about $6,000 a week. To meet this goal, the co-op needed 350 members, and each member would have to spend an average of $20 a week at the co-op.

Financing came from three sources. Member investments provided base capital of $10,000. In addition, the co-op secured a $10,000 long-term loan through the Ben and Jerry's Hot Fudge Venture Fund. Finally, a local bank loaned the group $20,000.

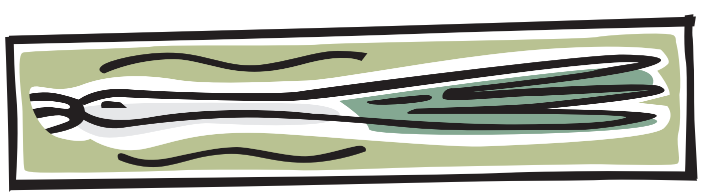
All the activity caught the attention of local media agencies. Before long newspapers and radio stations were reporting on the co-op's progress. By opening day in August, Midtown Food Co-op had 400 members. The co-op relied heavily on volunteer labor, as well as paid staff. It communicated with members via e-mail, a biweekly newsletter, and a website. Members invested $25 per year and received discounts on purchases.

In the following years, membership grew, but sales were sluggish. By 2004 the co-op had about 500 members, but sales were less than $10 per week per member. The co-op found itself $80,000 in debt. It owed money to vendors, as well as to the state for sales tax. The co-op held a benefit, which enabled it to pay off some of its debt, but it was unable to remain open. Midtown closed its doors in August 2004.

A former manager believes that that co-op could have done more profit analysis and kept better track of inventory. She also believes the store should have raised prices and lowered membership discounts.

Co-op development professionals cite additional issues. While they were able to generate initial support from the community in a short time, organizers skipped over a lot of critical planning stages—including market and feasibility studies. Those studies would have shown organizers what they could realistically expect from the community regarding sales. They might also have learned that their chosen location wasn't ideal. Additionally, professional co-op development specialists might have encouraged more member investment for more equity and a more stable financial base.

Midtown might also have more deeply considered its long-term value and role in the community. It might have spent more resources in meeting community needs. Instead, it ran out of time and money before it could realize a stronger vision.



CHAPTER 8

Co-op Conversions

An exciting new development for the food co-op sector is the conversion of some noncooperative businesses into consumer- or employee-owned co-ops. Although any kind of business can become a co-op, this chapter focuses on sole proprietor conversions to consumer-owned co-ops. If you'd like more information regarding conversion to an employee-owned cooperative, visit the National Center for Employee Ownership at *http://www.nceo.org* or the U.S. Federation of Worker Cooperatives at *http://www.usworker.coop*.

There can be tax advantages to the sole proprietor for converting into either a consumer- or employee-owned co-op. Sole proprietors will need to decide which co-op type makes the most sense for their businesses.

A conversion can also be an excellent exit strategy for owners wishing to sell their businesses while keeping them thriving as community assets. Other people who benefit from conversions are long-term suppliers, customers, and staff—all of whom have a stake in the success of the business.

A sole proprietor conversion is not as complicated as starting a new food co-op. The business is not starting from scratch. Its reputation in the community and its track record are known. The transition to co-op ownership is usually not a huge change because many operational systems are already in place. But the unique function of cooperatives for their members and their communities usually requires a thorough approach to conversion, involving outreach as well as financial and legal due diligence.

A successful co-op conversion requires advice from professionals with a deep understanding of cooperative business practices, as well as from those who offer specific business planning services. Those undertaking a co-op conversion will probably need assistance with financial planning, financing, legal procedures, and business evaluation. They might want to hire a third-party facilitator to help with the timeline and planning and to assure that stakeholders are properly included in the conversion process.

FYI: Tax Advantages for Employee-Owned Conversions

When converting a business into an employee-owned co-op, sellers and future employee-owners will want a full understanding of the IRS's 1042 election, or rollover option. This option lets a business owner shelter capital gains by selling the business to a worker-owned co-op. After the sale, the seller must invest the proceeds in "qualified replacement property" no more than 12 months after the closing date on the stock buyout. It is important to get legal advice on this process.

Steps to Co-op Conversion

Create a Steering Committee

Those considering a co-op conversion should organize a steering committee to gather information and assess the potential for cooperation and the feasibility of conversion. The group will do preliminary work to learn what needs to be done legally and financially.

Generate Public Support

Knowing whether your community will support a cooperative with its equity and patronage is an important part of the conversion process. The steering committee must educate people on cooperatives and how they can benefit the community. This kind of outreach usually involves the coordinated efforts of numerous people. For more detailed information about assessing community interest and communicating your plans, see Chapter 4.

Incorporate a Co-op

By incorporating a co-op, you create a legal entity with the ability to purchase the existing business. Incorporation offers legal protection for those involved in the conversion. It also allows the steering committee to appoint a board of directors to govern the co-op. This step should be carried out in consultation with a lawyer, because states have different laws regarding co-op incorporation.

For more detailed information on incorporation, legal issues, and creating co-op articles and bylaws, see the *Legal Primer on the Formation of Retail Consumer Food Co-ops* from the Food Co-op Initiative, *http://www.foodcoopinitiative.coop/resources/toolbox.*

Appoint a Board of Directors

A board of directors (which could be comprised of people from the steering committee) will undertake the formal and legal tasks related to the conversion. The board will do the following:

- Endorse policies to guide the co-op
- Approve the budget
- Ensure the financial viability of the co-op
- Hire and monitor the co-op's general manager
- Oversee committees accountable to the board

For more information about the role of co-op boards, see Chapter 1. For more information about the transition to governing, see the *Governance Toolbox,* available on CGIN: *www.cgin.coop/toolbox.*

Establish Articles and Bylaws

Articles of incorporation are legal documents filed with the state. They create the corporation as a distinct legal entity. Bylaws are the "constitution" of the co-op. They cover the rights and responsibilities of membership, how future retained earnings will be distributed, who can become a member of the co-op, voting rights, equity requirements, and governance positions. These documents should be created in consultation with a lawyer, because laws vary from state to state.

For more information about creating articles and bylaws, see Chapter 5. Also see the *Legal Primer on the Formation of Retail Consumer Food Co-ops* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox.*

Appraise the Business and Conduct Due Diligence

Although you probably already know a lot about the business you are considering converting, including its products, services, and competition, it is critical to get an accurate valuation of the business. Conduct a market study and general feasibility research to determine whether the business has limited potential or is poorly located. A market study might also show that a well-planned co-op could draw sales and exceed the existing store's capacity.

Have a certified accountant conduct other in-depth research, especially via the records of the business, to get a true picture of its annual sales, payroll, profits and losses, and customer base. Evaluate the physical plant. Additionally, be clear that your co-op is interested in buying only the assets of the business, not any existing liabilities.

Business valuation can be one of the most sensitive activities in a co-op conversion. Most independent business owners dedicate their whole careers to building their businesses, and each party in a conversion might have a different sense of a business's value. It is essential to get an independent review of the business based upon its history as well as future prospects. However, dollar value is only one part of appraising the business. Other factors (operational synergies, status in the community) can increase value and the final price of the business.

For more information about gathering information and other feasibility issues, see Chapter 4.

FYI: Privacy versus Transparency

The co-op business model encourages transparency. Co-ops share relevant information about financial performance with members, invite input from members and customers, hold annual meetings, and encourage other forms of member involvement. To a sole proprietor, by contrast, sharing information about the business can feel invasive.

During a co-op conversion, it's important for both parties to recognize that the private business affairs and life's work of the sole proprietor are being deeply scrutinized. Even if the seller-owner is enthusiastic about the co-op conversion, the experience can be unsettling. It's important to balance the need for transparency with the seller's right to confidentiality.

Recruit Members

Conversion to a consumer-owned co-op will involve a membership drive. (Conversion to an employee-owned cooperative will probably not.) Raising equity for your co-op is serious business, since equity is the capital base from which your co-op derives its ability to grow into the future. Securing member capital is also key to getting financing from other sources. It is critical that new members understand the responsibilities of member-ownership and what their participation means to the success of the venture.

For more information on signing up members, see Chapter 5. For more detailed information about setting member equity levels and creating a membership system, see the *Member Equity Toolbox: Structuring Capital to Meet Present and Future Needs* from the Food Co-op Initiative: *http://www.foodcoopinitiative.coop/resources/toolbox.*

Secure Other Financing

In addition to member equity, the co-op will need funds from financial institutions. Whether the seller-owner wants to cash out of the business immediately or phase out over a course of years will influence your financing package.

For more information on co-op financing, see Chapter 5. See also the *Member Equity Toolbox: Structuring Capital to Meet Present and Future Needs* and the *Member Loan Toolbox,* from the Food Co-op Initiative *http://www.foodcoopinitiative.coop/resources/toolbox* and the *Expansion and Relocation Toolbox,* available on CGIN: *http://www.cgin.coop/toolbox*.

Draft a Purchase Agreement

Once you have done due diligence on the records of the business and have located financing, it is appropriate to discuss terms of the sale, for instance, how the co-op will retain staff and benefits. Then have an attorney draft a legally binding purchase agreement on behalf of the co-op.

Purchase Assets and Dissolve the Old Business

Once negotiations with the seller-owner are complete, it is time to purchase the assets. Once all the documents have been signed, the co-op is ready to begin its transition. Although signing the necessary documents makes the conversion official, you will experience an adjustment period as management, staff, and members acclimate to their new roles and responsibilities. It is important that the co-op implement staff training, member education, and community outreach.

Making the Transition

Prepare the Staff for Reorganization

Employees of a newly converted co-op will probably have a lot of questions and concerns about their future with the organization. It is important for the co-op to listen to and address their concerns and to communicate the benefits of the change effectively. The co-op must establish a relationship of trust and integrity with employees and foster an atmosphere of working toward common goals.

It is quite possible that the change in management or staffing will alter the workplace dynamic. Co-op management must be mindful of this possibility. Through training and feedback, it must work with employees to provide for a positive long-term work environment and job security. Employees need to have confidence in the future of the business to work as a team.

If the co-op incorporates as an employee-owned business, the reorganization process will be more intensive. The business will have to set up ownership investment and financing plans, decision-making procedures, and management structures.

FYI: The Sole Owner's Exit Strategy

Some owners may desire an active role in the cooperative after a conversion. Others may have no interest in continuing the relationship. Each approach has benefits. Keeping the former owner involved retains valuable knowledge and leadership. Ending the relationship offers a new start. Determining what is right for your co-op conversion will require agreement from both parties. It is important to address any conflict of interest and how the seller's future involvement will be structured. You may also wish to secure legal advice about this issue. No matter what the sole owner and the cooperative negotiate, terms will need to be secured through formal agreements.

Establish the Co-op Identity

The new co-op will want to establish itself as such in shoppers' minds. Its outreach, advertising, and educational materials should project a consistent image. Communications vehicles (some of which may be adapted from the original business) might include a website, ads, brochures, press releases, newsletters, directory listings, letterhead, business cards, and in-store signage. Every contact with customers should help solidify the co-op's identity. All materials should clearly demonstrate the store's commitment to its principles, mission, and vision.

Train Staff

Now is the time to build strong relationships with staff. Train them in customer service standards. Your training should reflect the values of the organization, including its mission statement and consumer values and beliefs.

Note to Business Owners and Cooperators

Co-op conversions are new territory for the food co-op sector. We'd appreciate feedback from groups who have been through this process so we can include your input in future editions.

case study

Basics Cooperative

Janesville, Wisconsin
www.basicshealth.com

Before Basics Cooperative became a natural foods co-op in 2004, it had been a beloved, privately owned mainstay of the Janesville community for more than two decades. When the owner died unexpectedly, his son was charged with taking care of his father's assets. The son cared deeply about the fate of the business his father had devoted himself to. He wanted to do what was best for it and for the community. A lawyer, he was not interested in owning or running the store himself. So with the help of others, he converted the independent business to a cooperative.

Organizers established a five-member board of directors. The group met biweekly, and the whole deal was put together in about six months. Organizers did not conduct a feasibility study because Basics was a profitable business. Organizers believed it would continue to be profitable as a cooperative.

The co-op did all its member recruitment with existing customers. It used flyers and community question-and-answer sessions. Despite widespread support for the co-op, recruitment was slow. Organizers set a goal of signing up 2,000 members but had recruited only about 500 by the time of the conversion. What that meant for the co-op was that the seller financed more of the sale.

After incorporation, the co-op hired a lawyer to negotiate the terms of the purchase. The value of the store was supported by a valuation report prepared by an outside accounting firm. The new co-op purchased the stock of the existing corporation. The corporation was then dissolved.

After the sale, the co-op made no changes to facilities or operations. The owner's son remained involved as a member of the board of directors. The board hired an able staff person as general manager, and directors attribute her skills to a painless transition as well.

Basics Cooperative offers some tips for groups considering a co-op conversion:

- Elect a board of directors as soon as possible
- Hire good legal and accounting counsel
- Do as much research as possible
- Make the membership drive a top priority
- Involve and excite management and staff
- Develop strong marketing materials and make a big initial splash with customers
- Continually educate customers

By 2010 Basics had 2,200 members and had embraced its identity as a cooperative. Although some of the shifts are subtle, shoppers now feel more a part of the store because they own it. The co-op has a formal stated mission to serve the community. Its outreach to schools and other community groups has increased. It has built strong networks with producers and other local businesses to promote the local economy and sustainability.

Basics Cooperative at a Glance

Year opened as a sole proprietorship:	1981
Year incorporated as co-op:	2004
Year opened as co-op:	2004
Number of members at opening:	500
Number of members in 2010:	2,200
Member equity investment:	$150 per household
Member loans:	none
Member equity:	$50,000
Financing:	seller financed
Number of staff at opening:	35
Number of staff in 2010:	45
Retail square feet:	10,000
First-year sales:	$2.1 million
2008 sales:	$2.6 million

Glossary

articles of incorporation: the founding legal documents of a corporation. When its articles of incorporation are approved by the appropriate state agency, a corporation begins its own distinct existence, subject to the laws and regulations affecting that type of corporation. Articles of incorporation should set forth the name of the cooperative, the cooperative's duration and address, the purpose of the co-op, how membership works, what capital is required of members, and what happens to the co-op's assets upon dissolution.

bylaws: rules that specifically describe how a co-op will conduct its affairs. While bylaws need to be more specific than articles, it is wise to avoid being *too* specific. Bylaws should specify procedures that will be used in approving members, distributing net income, paying back members' capital, and voting, as well as the number and responsibilities of directors and other matters.

board of directors: the elected body responsible for the actions of a corporation

capital: money used in a business, whether supplied by owners or borrowed. *Capital* most typically refers to money contributed to a business by owners or stockholders. In accounting, *capital* refers to the remaining assets of a business after all debts and amounts owed to others have been deducted. Member equity is also capital. See "equity" in this glossary for more information.

corporation: a legal entity created under state laws. Once established, a corporation has its own legal powers, rights, and liabilities distinct from those of its owners or managers.

dividends: amounts paid to business owners based on their investments. Typically, dividends represent a share of profits paid to shareholders proportionate to the shares held in a corporation. Cooperatives pay dividends based on owner patronage. See "patronage rebate or patronage refund" in this glossary for more information. Co-ops may also pay dividends on preferred shares as a means to encourage member investment.

equity: ownership interest in a business. Equity is made up of investments by owners (members) and the cumulative profit of the business (capital). Equity is most easily calculated by subtracting all liabilities (amounts owed) from all assets (amounts and property owned).

incorporate: to establish a business as a legal entity. Incorporation typically entails filing articles of incorporation and bylaws with the state to conform to a corporate statute.

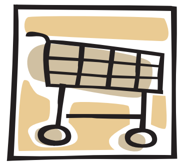
net savings: total income (sales) less total expenses; also called profit and or net income

patronage rebate or patronage refund: a distribution of profits to members, proportionate to members' use of or purchases from the co-op; also called patronage dividends

securities laws: laws that govern how businesses can take investment from potential owners

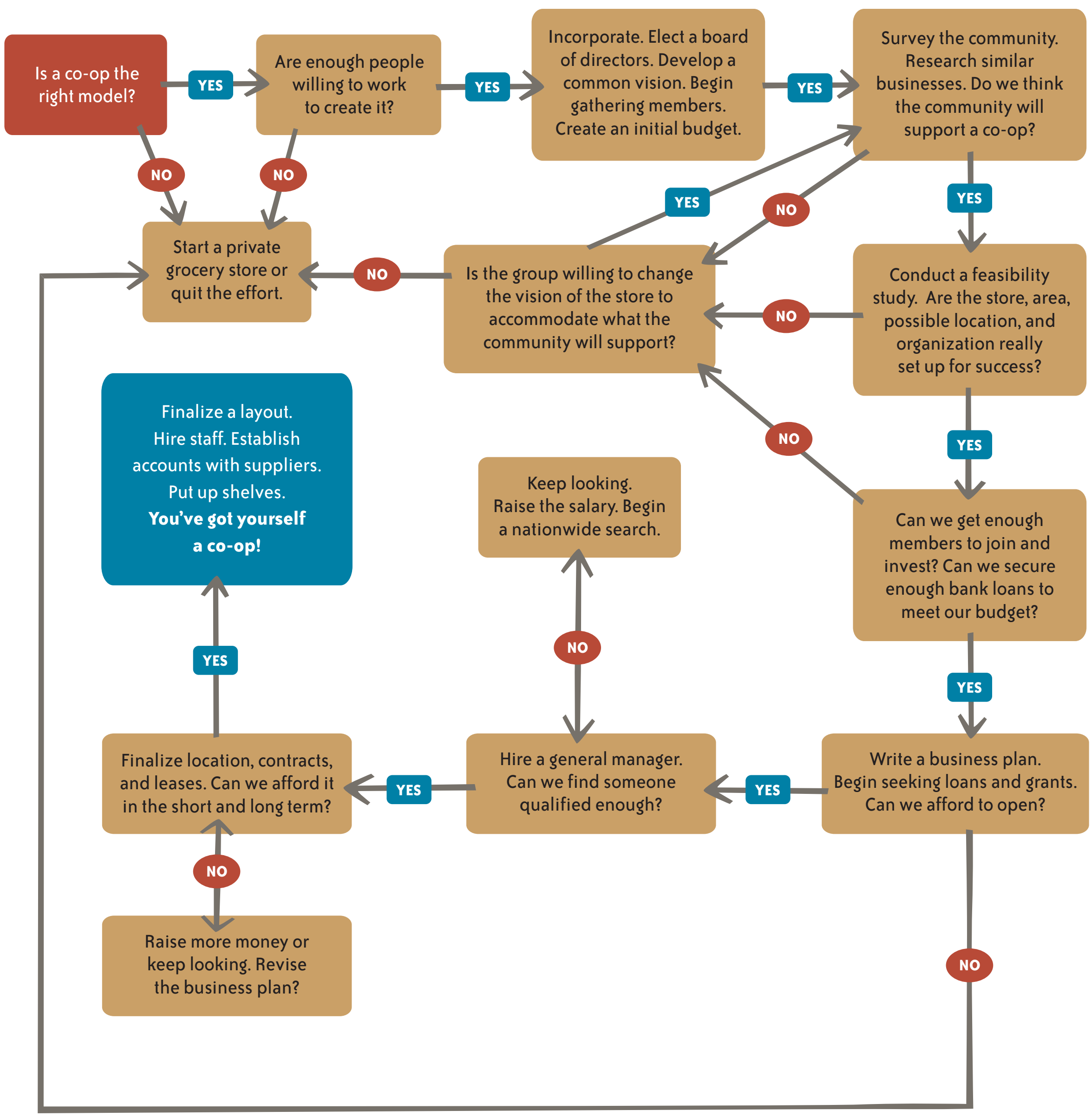
shares or membership shares: investment units sold to co-op members. Shares are like stock in a traditional business, but because of special rules, membership shares are not subject to the same regulations that govern stock. For that reason, most co-ops prefer to use the term *share* in reference to member investments.

steering committee: a committee responsible for guiding work, such as researching and planning a new co-op. A steering committee is typically elected or selected by those interested in researching the feasibility of a new co-op.



How to Start a Food Co-op

adapted from Kitsap Community Food Co-op, Kitsap, Washington



Organizations to Contact

CDS Consulting Co-op

http://www.cdsconsulting.coop

CDS Consulting Co-op is a network of independent consulting professionals. Consultants specialize in helping food co-ops achieve growth, increase profitability, improve board leadership, strengthen management, and more fully serve members and their communities.

Cooperation Works!

http://www.cooperationworks.coop

A cross-sector cooperative development network. Click on "members" on the website to get a list of regional co-op development agencies.

Cooperative Grocers' Information Network (CGIN)

http://www.cgin.coop

CGIN is a nonprofit association of North American food co-ops. Its website offers general information, resources, and links for food co-ops, as well as a library of materials accessible only to CGIN members. CGIN also operates a listserve open to anyone interested in food co-ops.

***Cooperative Grocer* magazine**

http://www.cooperativegrocer.coop

Cooperative Grocer is published every other month. Readers will find articles on operating co-ops, relocation and expansion projects, and other topics of interest to food co-ops. The website offers an index of back issues and articles, many of which are available online.

Food Co-op Initiative

http://www.foodcoopinitiative.coop

Food Co-op Initiative is a nonprofit foundation created to provide resources and support for communities that want to start food co-ops.

International Co-operative Alliance

http://www.ica.coop

The International Co-operative Alliance brings together cooperatives from more than 100 countries. The website provides general information about cooperatives around the world.

National Cooperative Bank
http://www.ncb.coop

The National Cooperative Bank is dedicated to strengthening communities nationwide through the delivery of banking and financial services to cooperatives.

National Cooperative Business Association
http://www.ncba.coop

NCBA is the leading national association representing cooperatives of all types and in all industries in the United States.

National Cooperative Grocers Association
http://www.ncga.coop

NCGA offers business services to cooperatives throughout the United States. It helps natural food co-ops optimize operational and marketing resources, strengthen purchasing power, and offer more value to co-op owners and shoppers.

University of Wisconsin Center for Cooperatives
http://www.uwcc.wisc.edu

The University of Wisconsin Center for Cooperatives pursues a research, educational, and outreach agenda that examines cooperative issues across multiple business and social sectors. The agenda encompasses all aspects of the cooperative business model, including development, finance, structure, and governance.

Further Reading

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Gutknecht, Dave, and Karen Zimbelman, editors. *Challenges to the Cooperative Board of Directors. Cooperative Grocer* magazine, 1996. A collection of ten articles for co-op boards about their role and handling key functions. http://www.cgin.coop/toolbox/challenge_pub

Hill, Patricia, Mary Jean McGrath, and Elena Reyes. *Cooperative Bibliography.* University Center for Cooperatives, University of Wisconsin Extension, 1981. An annotated and exhaustive guide to works in English on cooperatives and cooperation.

McLanahan, Jack, and Connie McLanahan, editors. *Cooperative/Credit Union Dictionary and Reference.* Cooperative Alumni Association, 1990. An excellent reference to all aspects of cooperative activity.

National Cooperative Bank. *How to Organize a Cooperative.* National Cooperative Bank, 1992. An adaptation of *How to Start a Cooperative*, published by the USDA, adapted for different types of co-ops.

National Cooperative Bank. *Draft Articles and Bylaws.* National Cooperative Bank, 1994. A guide to recommended language for co-op articles of incorporation and bylaws.

National Society of Accountants for Cooperatives. *NSAC Resource Guide.* National Association of Accountants for Cooperatives, 1994. A listing of resources specifically addressing financing, accounting, taxation, and legal issues applicable to cooperatives.

Rasmussen, Eric. *Financial Management in Co-operative Enterprises.* Co-operative College of Canada, 1975. A comprehensive overview of financing in cooperatives, including basics and details about feasibility studies, rate-of-return and break-even analysis, and cash management.

Roy, Ewell Paul. *Cooperatives: Development, Principles and Management.* Interstate Printers and Publishers, 1981. A university textbook that comprehensively reviews the theory, history, and practices of co-ops of all types.

Schaars, Marvin A. *Cooperatives, Principles and Practices.* University of Wisconsin, Madison, 1980 (revised). An overview of cooperative structure and operational applications, mostly oriented toward agricultural and marketing co-ops.

Swanson, Walden, and Mary Myers. *Business Planning for Cooperatives.* Cooperative Development Services, 1991. A detailed guide to preparing a business plan for a cooperative.

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USDA/RBCDS Cooperative Services. *Organizing and Conducting Cooperatives' Annual Meetings.* Cooperative Information Report 21, 1983 (revised). A guide to preparing for and holding an annual meeting.

USDA/RBCDS Cooperative Services. *How to Start a Co-op.* Geared toward marketing co-ops, this video reviews the steps involved in starting a co-op.

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CGIN board members as of October 2010

John Eichholz, Treasurer	Franklin Community Co-op
Dan Gillotte, President	Wheatsville Food Co-op
Travis Hance	Syracuse Real Food Co-op
Jane Harter	East End Food Co-op
Alysen Land	Ozark Natural Foods
Deirdrie Lang	Kootenay Country Store Co-op
Doug Walter, Secretary	Davis Food Co-op

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